

# Capital Reporting Company

BEFORE THE COPYRIGHT ROYALTY JUDGES  
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Copyright Royalty Board  
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In the Matter of: :

MECHANICAL AND DIGITAL  
PHONORECORD DELIVERY RATE  
ADJUSTMENT PROCEEDING.

: Docket No.:  
: 2006-3-CRB DPRA  
:  
: Volume 1 - A.M.  
-----: (Pgs. 1 - 117)

Washington, D.C.

Monday, January 28, 2008

The following pages constitute the  
proceedings held in the above-captioned matter,  
held at the Library of Congress, Madison Building,  
101 Independence Avenue, Southeast, Washington,  
D.C., before Shari R. Broussard, RPR, of Capital  
Reporting Company, a Notary Public in and for the  
District of Columbia, beginning at approximately  
a.m.

1 A P P E A R A N C E S

2 Copyright Royalty Tribunal:

3 CHIEF JUDGE JAMES SLEDGE  
4 JUDGE WILLIAM ROBERTS  
5 JUDGE STANLEY C. WISNIEWSKI

6

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1 P R O C E E D I N G S

2 CHIEF JUDGE SLEDGE: The United States  
3 Copyright Royalty Judges are assembled. The order  
4 for the court this morning is the mechanical rate  
5 proceeding to set the rates and terms in  
6 Section 115.

7 All with matters to be presented before  
8 this court please come forward. We will begin  
9 today with the Motion for Referral filed by DiMA  
10 and proceed from there to the opening statements.  
11 Please be seated.

12 A little bit of organizational at the  
13 beginning of this proceeding. For those of you  
14 that have not been present in any prior proceedings  
15 in this room, there is a cafeteria on the sixth  
16 floor, there are restrooms just outside in the  
17 corridor by the elevators on this floor. I hope  
18 you've had success in getting your materials in.  
19 If not, sorry, we can't help you.

20 (Laughter.)

21 CHIEF JUDGE SLEDGE: Materials and  
22 security and facilities are matters that are

1 something over which we have very little input.

2 We announced in our scheduling order our  
3 daily schedule. If it's not clear in there, we  
4 will try to take a break at noon, try to resume at  
5 1:00 depending on where we are with the witness at  
6 that particular time, and we'll try to conclude  
7 each day around 4:30. We went to 5:00 in our last  
8 proceeding, and that seemed to interfere with all  
9 that has to be done outside the courtroom, so we  
10 went back to our initial schedule of 4:30 to try to  
11 permit time to accommodate all the other things  
12 that you and us have to do outside of here.

13 I believe that covers our administrative  
14 matters. We will begin with our motion by DiMA for  
15 referral. Mr. Laguarda?

16 MR. LAGUARDA: Thank you, Your Honor.

17 JUDGE ROBERTS: Mr. Laguarda, I'd remind  
18 you, as well as all the other litigants, to speak  
19 as loudly as possible. Unfortunately, the  
20 acoustics in this room are not all that great. So  
21 if you could speak up, I think we would all  
22 appreciate it.

1 MR. LAGUARDA: Thank you.

2 CHIEF JUDGE SLEDGE: This room is  
3 designed to have a sound system, and if somebody  
4 sees it, please let us know.

5 (Laughter.)

6 MOTION FOR REFFERAL BY COUNSEL FOR DiMA

7 MR. LAGUARDA: Thank you, Your Honor.  
8 I'll do my best.

9 May it please the Court, Fernando  
10 Laguarda for the Digital Media Association.

11 The issue on our motion is the pure  
12 question of statutory interpretation, that is,  
13 whether the term "digital phonorecord delivery" in  
14 Section 115 of The Copyright Act should be  
15 interpreted to include interactive streaming.

16 The motion is novel in that no court or  
17 other tribunal has addressed it.

18 As presented in the motion, the question  
19 is does interactive streaming of a sound recording  
20 constitute a digital phonorecord delivery under  
21 Section 115 of the Act.

22 If it is a digital phonorecord delivery,

1     then Section 115 applies, and rates and terms  
2     should be set by this court, as the copyright  
3     owners propose. If it is not a digital phonorecord  
4     delivery, then the court need not set rates.

5             DiMA defines interactive streaming as the  
6     playing of a specific sound recording in response  
7     to the listener's request without the creation of  
8     an audio file that remains accessible on the client  
9     computer beyond the playing of such sound  
10    recording.

11            In Section 115, digital phonorecord  
12    delivery is defined as the individual delivery of a  
13    phonorecord by digital transmission of a sound  
14    recording, which results in a specifically  
15    identifiable reproduction by or for any  
16    transmission recipient of a phonorecord of that  
17    sound recording. Interactive streaming does not  
18    deliver a phonorecord.

19            The word "phonorecord" appears twice in  
20    the definition of digital phonorecord delivery.  
21    The Act clearly defines phonorecord as a material  
22    object in which sounds are fixed and from which the

1 sounds can be perceived, reproduced or otherwise  
2 communicated. The definition contemplates  
3 something that is fixed, something delivered that  
4 the recipient can play at will.

5 Interactive streaming does not let a user  
6 play a fixed record whenever he wants to. Like a  
7 song heard on the radio, a song heard via  
8 interactive streaming cannot be rewind, played  
9 back or otherwise used again. It is, therefore,  
10 not fixed for a period of more than transitory  
11 duration.

12 The Act provides that a work is fixed  
13 when its embodiment is sufficiently permanent to  
14 allow it, or stable to permit it to be perceived or  
15 communicated for a period of more than transitory  
16 duration.

17 In looking at the structure of the Act  
18 and the definitions, it's clear that digital  
19 phonorecord delivery was defined to confirm the  
20 traditional commonsense definition of delivering  
21 phonorecords. In other words, the intent of  
22 Congress was to maintain and reaffirm and not



1 expand mechanical rights, as technology permitted  
2 phonorecords to be delivered by wire or over the  
3 airways, rather than the traditional making of  
4 records, cassettes and CDs.

5 CHIEF JUDGE SLEDGE: That's curious. Not  
6 intended to expand rights when it goes from  
7 something you hold in your hand to something that's  
8 digital? It seems like an expansion, doesn't it?

9 MR. LAGUARDA: It's an expansion of --  
10 technology expands the ability to deliver the  
11 phonorecord. It does not expand the rights  
12 associated with it.

13 What Congress said, and the Senate Report  
14 says, is that the purpose of creating a digital  
15 phonorecord delivery mechanism and rate setting  
16 mechanism for that under 115 is to allow for the  
17 compulsory license to be used in circumstances  
18 where phonorecords are delivered digitally.

19 The rights in the phonorecords are the  
20 same rights that existed before the amendment of  
21 the statute, and that's where the legislative  
22 history provides some guidance.

1                   It's not an expansion of the rights.  
2           It's a recognition that technology can distribute  
3           and deliver, as the definition provides, a  
4           phonorecord to an end user. But what is being  
5           delivered, what is being distributed is a  
6           phonorecord, like a cassette, like a CD, like a  
7           record, and that's what's clear.

8                   Now, the only federal court that has  
9           considered anything related to this issue  
10          considered the question of whether downloading a  
11          musical file constitutes public performance, and  
12          that is the Southern District of New York in  
13          connection with rate setting for the ASCAP, a  
14          performing rights organization.

15                   CHIEF JUDGE SLEDGE: Is that the citation  
16          on page four of your motion?

17                   MR. LAGUARDA: Yes, Your Honor.

18                   CHIEF JUDGE SLEDGE: Your citation is  
19          incomplete and inaccurate. That's the Southern  
20          District of New York?

21                   MR. LAGUARDA: Yes, Your Honor. Senior  
22          Judge Conner in that case, Your Honor, considering

1 the question of whether there's a public  
2 performance in downloading. And that is, I would  
3 suggest, a very practical understanding of the  
4 statute. The question here is, and the definitions  
5 under the Copyright Act, the question here is  
6 whether a transmission that is delivering a  
7 performance to the end user is the distribution of  
8 a phonorecord. And as we are defining it and as  
9 the statute makes clear, merely transmitting a  
10 song, publicly performing it, does not constitute a  
11 digital phonorecord delivery, and that's the legal  
12 question that merits referral.

13 JUDGE ROBERTS: Mr. Laguarda, what's the  
14 meaning of streaming?

15 MR. LAGUARDA: The meaning of streaming  
16 is not a legal question. That's a question of, as  
17 we have defined it, transmitting a sound recording  
18 and a musical work over the Internet and publicly  
19 performing it more likely than not.

20 JUDGE ROBERTS: If we refer this question  
21 to the Register, will she not have to define what  
22 streaming is in order to answer the question on

1       whether interactive streaming does not result in a  
2       digital phonorecord delivery?

3               MR. LAGUARDA:   The real issue for the  
4       Register to grapple with is whether there is a  
5       phonorecord, whether a phonorecord is delivered,  
6       that is, if a transmission, as we have defined  
7       streaming, does not result in the delivery of a  
8       phonorecord.

9               JUDGE ROBERTS:   You say how you define  
10       it.   The question I'm asking, though, is isn't the  
11       Register going to have to give a definition to  
12       streaming in order to make a determination of  
13       whether there is a --

14               MR. LAGUARDA:   Yes, and that's the  
15       definition that we have provided; simply the  
16       transmission of a sound recording to an end user  
17       that does not result in the creation of a  
18       phonorecord that the user can then use.

19               There is no delivery of a phonorecord in  
20       streaming because streaming is the rendering of an  
21       audio file from a server to the user, and there are  
22       copies, as the copyright owners suggest in their

1       opposition, there may be lots of different ways and  
2       mechanisms to deliver the stream to the end user.  
3       But the key point is that if the end user does not  
4       get a phonorecord, the end user doesn't get  
5       something like a cassette, a record or a CD, then  
6       it's not a digital distribution, digital  
7       phonorecord delivery that is defined in the Act,  
8       and that's the key question.

9               Yes, we are proposing the raw facts that  
10       are necessary to answer the question, but it's not  
11       dependant on the technology that is involved  
12       because the ultimate question is what does the user  
13       get. Does the user get a phonorecord delivered to  
14       them for their use and enjoyment?

15              JUDGE WISNIEWSKI: Well, Mr. Laguarda,  
16       just to follow-up on that, and I don't mean to  
17       interrupt Judge Roberts' colloquy here, but do you  
18       have agreement among all the parties as to your  
19       definition of interactive streaming?

20              MR. LAGUARDA: No, Your Honor, we do not.  
21       But there is agreement --

22              CHIEF JUDGE SLEDGE: This seems to come

1 back to when he asked you if the Register would  
2 have to define that. You went on to go on to talk  
3 about other things, but the answer is yes?

4 MR. LAGUARDA: The answer is yes, Your  
5 Honor, the Register has to define it, and that's  
6 why we proposed a definition in the motion. The  
7 definition itself is the simple definition of  
8 streaming the transmission of the sound recording  
9 to the end user. There are many ways --

10 JUDGE WISNIEWSKI: So you're really  
11 proposing two questions for the Register then,  
12 aren't you?

13 MR. LAGUARDA: No, because the definition  
14 of streaming is not a legal question in and of  
15 itself.

16 JUDGE WISNIEWSKI: But you admit the  
17 Register has to determine what that definition is.

18 MR. LAGUARDA: No, the Register, as with  
19 Ring Tones, the Register has to understand the  
20 general facts that are the context for answering  
21 the question of law, but the question of law is  
22 simply whether an activity that does not distribute

1 a phonorecord constitutes a digital phonorecord  
2 delivery.

3 JUDGE WISNIEWSKI: Well, let's assume  
4 that the Register were to take your definition of  
5 interactive streaming and, in fact, decide this  
6 legal question. How far does that advance the ball  
7 for these proceedings since you don't have any  
8 agreement on what that definition is? Don't we  
9 still have to set a rate for where you don't have  
10 an agreement?

11 MR. LAGUARDA: No, Your Honor. For the  
12 distribution of the phonorecord to an end user  
13 there is at least -- there are three proposals  
14 before the court as to what rates should be if  
15 there's a phonorecord that's delivered.

16 The parties are in agreement with respect  
17 to that question. That is, where there is a  
18 phonorecord delivered, the mechanism of the  
19 transmission is what the copyright owners are  
20 raising. They are saying that where the end user  
21 doesn't get a phonorecord, there should still be a  
22 rate set in this proceeding. And the question of

1 law is whether it's enough to argue all of these  
2 factual matters and create a factual basis for  
3 setting a rate, or whether the legal question has  
4 to be answered that the transmission alone, without  
5 the creation of a phonorecord, is within the  
6 jurisdiction of rate setting under 115.

7 And I think that resolving the question  
8 to your inquiry, Your Honor, will make it easier  
9 for this proceeding because other than referring  
10 it, we will have a situation where the court will  
11 engage in rate setting and the copyright office  
12 will have an opportunity to answer the question at  
13 the end rather than before the parties clearly  
14 understand what the legal landscape is in defining  
15 their rate request.

16 At the moment there is no clarity for  
17 understanding the scope of the statute and what is  
18 contemplated by the meaning of the digital  
19 distribution by digital phonorecord, and that's  
20 why, to answer I think the question that concerns  
21 you, it's more efficient for these proceeding to  
22 resolve it now. And the work that has to be done



1 in terms of the definition is no different than on  
2 any referral of the question of law or appeal of a  
3 question of law. The facts are necessarily going  
4 to be defined in a manner that allows the question  
5 of law to be answered. But we are not proposing  
6 that this is an issue that requires delving into  
7 how the stream occurs because the point is what the  
8 user gets, and that is not a phonorecord, and that  
9 is why Section 115 doesn't apply.

10 CHIEF JUDGE SLEDGE: The definition of  
11 interactive streaming will be based on evidence  
12 presented in this proceeding?

13 MR. LAGUARDA: The definition of  
14 interactive streaming if a digital phonorecord  
15 delivery contemplates an activity where the user  
16 does not get a phonorecord, then the issue of what  
17 is interactive streaming and how a rate will be set  
18 is a question that could be addressed in this  
19 proceeding, Your Honor, but it's not in the record  
20 right now.

21 CHIEF JUDGE SLEDGE: That didn't answer  
22 my question.

1 MR. LAGUARDA: Perhaps if you'd repeat  
2 it.

3 CHIEF JUDGE SLEDGE: Will that definition  
4 be determined by the evidence presented in this  
5 proceeding?

6 MR. LAGUARDA: The definition of  
7 interactive streaming? The parties have proposed,  
8 both the copyright owners and RIAA, have proposed  
9 definitions of interactive streaming, but they have  
10 not proposed any evidence supporting it, or to the  
11 copyright owners justifying any of the technical  
12 issues that they propose need to be addressed.

13 After the legal question is answered as  
14 to whether or not a statute contemplates rate  
15 setting for that activity, then, yes, if the answer  
16 is it does, then this proceeding needs to address  
17 the question of what type of activity qualifies for  
18 a rate. Does that answer the question?

19 CHIEF JUDGE SLEDGE: Yes, and it raises  
20 several others. As you say, it's not addressed in  
21 the direct cases of anyone. How then will it be  
22 presented to the Court for determination?

1 MR. LAGUARDA: Well, from DiMA's  
2 perspective it need not be presented because the  
3 question, as a matter of law, will be answered by  
4 the Register that no rate need be set and,  
5 therefore, no record needs to be created.

6 CHIEF JUDGE SLEDGE: Well, that assumes  
7 your argument, that has not seemed to be very  
8 persuasive so far, that that legal question does  
9 not require a definition of legal streaming to  
10 answer the legal question you proposed.

11 MR. LAGUARDA: Well, Your Honor, if the  
12 Register were to answer the question affirmatively  
13 that a rate needs to be set for interactive  
14 streaming, then the parties need to put a record  
15 before the Court in order to answer that question.  
16 It currently does not have a sufficient record to  
17 answer the question of what is interactive  
18 streaming.

19 But to get back to the point that you  
20 were making, the question of law is a question of  
21 what is a digital phonorecord delivery. That's the  
22 question of law.

1           The activity for which the copyright  
2 owners request rate setting is the transmission of  
3 a sound recording to an end user. They have a  
4 definition of it. That transmission does not, as  
5 they define it or as we define it, the point is  
6 that the mere transmission does not deliver a  
7 phonorecord to an end user.

8           Now, the copyright owners might argue  
9 that there are circumstances in which there is a  
10 phonorecord delivery, and that's a question of fact  
11 that can be answered in this proceeding, and there  
12 may be a rate for that activity. But the  
13 transmission of a sound recording, of an audio file  
14 played to a user, in and of itself, does not  
15 deliver a phonorecord.

16           The statute is clear on the point that  
17 the creation of the digital phonorecord delivery  
18 category was not intended to create by itself new  
19 rights. It was intended to recognize the  
20 possibility that technology would allow  
21 phonorecords, cassettes, CDs and traditional vinyl  
22 records to be delivered to end users. That

1 activity is not what is contemplated in any way by  
2 streaming no matter how it's defined.

3 So if the definition of streaming  
4 contemplates that the user gets a phonorecord, then  
5 that, of course, is an issue that is subject to  
6 rate setting. But the point is that streaming, no  
7 matter how it's defined, doesn't leave the end user  
8 with a phonorecord. There are copies that may be  
9 made, but all of those questions, all of those  
10 copies are beside the point with respect to the  
11 law.

12 The law is clear that there must  
13 eventually be a phonorecord distributed to the end  
14 user, and none of the definitions that avoid that  
15 question will result in an orderly rate setting  
16 proceeding before this court.

17 JUDGE WISNIEWSKI: Mr. Laguarda, since  
18 there's no agreement among the parties as how to  
19 define interactive streaming, why wouldn't we  
20 simply refer, instead of the question as you have  
21 framed it in your motion, the question as you have  
22 intimated the heart of it is, as whether the

1 playing of a specific sound recording in response  
2 to the listener's request without the creation of  
3 an audio file that remains accessible on the  
4 computer beyond playing of such a sound recording  
5 constitutes a DPD as a matter of law? Why  
6 shouldn't we refer that question rather than one  
7 that includes a definition over which there's some  
8 controversy?

9 MR. LAGUARDA: That sounds -- that  
10 sounds likely -- that is the question that we have  
11 presented, Your Honor, so I am comfortable with  
12 that referral, yes.

13 JUDGE ROBERTS: Mr. Laguarda, I'd like to  
14 ask you a question about the timing of this filing.

15 MR. LAGUARDA: Yes, Your Honor.

16 JUDGE ROBERTS: Why did you wait until  
17 January 7th of 2008 to ask for this referral? This  
18 was certainly an issue present for your members  
19 well before this, going back to I guess at least  
20 2001, and why was this not asked to be referred at  
21 a much earlier time?

22 MR. LAGUARDA: The answer, Your Honor, as

1 we've said in our papers, is that we've been  
2 attempting to resolve that question, absolutely has  
3 been known to our members.

4 What hasn't been known to our members has  
5 been the development of the proceeding, the  
6 Register's intervening decision on Ring Tones,  
7 which discussed the relevance or the manner in  
8 which the copyright office views industry  
9 agreements as opposed to legal definitions, and  
10 these things have created uncertainty.

11 The parties have attempted in good faith  
12 to address them. By no means was it an attempt to  
13 cause confusion in the proceedings. It was an  
14 attempt in good faith to resolve the issue that had  
15 not reached fruition. And because these  
16 proceedings were commencing, we felt that we had  
17 to, had no choice but to put the issue before the  
18 court and to get a prompt referral from the  
19 copyright office.

20 JUDGE ROBERTS: Is it your position that  
21 the law permits referral of a novel question at any  
22 time in the proceeding right up to the moment of

1     our decision? In other words, are we compelled to  
2     refer to this question or any other question that  
3     may come up provided that it is before we render  
4     our determination?

5                 MR. LAGUARDA: No, Your Honor, I would  
6     not make the argument that this court should ignore  
7     the orderly conduct of its proceedings in any way.  
8     You have to make that determination. However, the  
9     statute and the rules clearly provide and encourage  
10    the referral process at any point subject to, of  
11    course, the determination of the judges as to its  
12    appropriateness.

13                With respect to timeliness here, the  
14    operative provision calls for referral as soon as  
15    possible. And here we have a situation where the  
16    parties were attempting to resolve this other than  
17    by referral and were unable to. And the simple  
18    fact is that the latter we wait to resolve the  
19    question, the more it will interfere rather than  
20    the less, and that's why it makes sense to do it  
21    now.

22                CHIEF JUDGE SLEDGE: How long have the



1 parties been trying to resolve this question?

2 MR. LAGUARDA: Your Honor, the question  
3 has been known to the parties at least since the  
4 beginning of the case and the parties have  
5 discussed it.

6 CHIEF JUDGE SLEDGE: Does it not go back  
7 to the passage of the amendments and the disputed  
8 matters since the --

9 MR. LAGUARDA: Yes, Your Honor.

10 CHIEF JUDGE SLEDGE: -- amendments  
11 passed?

12 MR. LAGUARDA: In terms of the statutory  
13 interpretation, yes. In terms of its relevance to  
14 the proceeding, when the direct cases were filed  
15 obviously was the first time the parties had an  
16 opportunity to realize that this was an issue  
17 presented by the different rate proposals, and it  
18 has required the attention of the parties to try to  
19 address it.

20 CHIEF JUDGE SLEDGE: That seems  
21 unbelievable.

22 JUDGE ROBERTS: Does this mean,

1 Mr. Laguarda, that you've been discussing this with  
2 the music publishers and songwriters up to the  
3 holidays, and then you realized over the holidays  
4 that you're not going to resolve this and that's  
5 why it got filed on January 7th?

6 MR. LAGUARDA: There were very serious  
7 discussions, Your Honor, leading up to the  
8 holidays, yes, and I believe that I should be able  
9 to address the contention that this motion has been  
10 filed for purposes of bad faith or delay under the  
11 federal rules of evidence by pointing out that  
12 there have been settlement discussions. I'm  
13 uncomfortable talking about the settlement  
14 discussions in detail, but I can tell you that  
15 those discussions, in terms of resolving this  
16 issue, were very serious and were very involved  
17 through the holidays, absolutely. And the problem  
18 presented for the parties in this proceeding is  
19 there is a Catch 22 between attempting to resolve  
20 this and the deadlines required to put on a case in  
21 an orderly manner, and so we are not trying to  
22 present the Court with the worst-case scenario,

1     which is conducting the hearings, putting on  
2     additional evidence, which will be required in  
3     order to define interactive streaming and get all  
4     of the technical matters out onto the record,  
5     reaching some conclusion and then having the issue  
6     addressed by the copyright office as part of an  
7     ultimate resolution. That would be the worst-case  
8     scenario, which we want to avoid. So given the  
9     choices, the better option is to refer the question  
10    now. It's not something that we do without  
11    recognizing the burden it creates for the copyright  
12    owners and for the Court.

13                 JUDGE ROBERTS: You've asked for a  
14    referral of interactive streaming. What about  
15    conditional downloads? Is there any issue there  
16    that that should be referred either at this point  
17    or some future date as well?

18                 MR. LAGUARDA: No, Your Honor, I don't  
19    believe that there is any dispute about the use of  
20    Section 115 to cover the distribution of  
21    phonorecords over which users have control even if  
22    it is for a restricted period of time.

1 JUDGE ROBERTS: So we don't have to worry  
2 about another motion for referral coming in on that  
3 matter?

4 MR. LAGUARDA: I believe that that is  
5 addressed by all of the parties in their cases and  
6 it is not an issue that requires any legal  
7 findings. If there are no further questions...

8 CHIEF JUDGE SLEDGE: Thank you.

9 MR. COHEN: Your Honor, may I?

10 CHIEF JUDGE SLEDGE: One moment.

11 Mr. Smith, do you have anything you want  
12 to add?

13 MR. SMITH: Your Honor, I think at this  
14 point we will -- if we have any comment, I think it  
15 probably makes more sense for the publishers to go  
16 first. We don't have a position on the referral  
17 motion itself.

18 CHIEF JUDGE SLEDGE: All right. You  
19 probably will not have another opportunity to say  
20 anything.

21 MR. SMITH: Thank you.

22 CHIEF JUDGE SLEDGE: All right.

1 Mr. Cohen?

2 REBUTTAL OF MOTION FOR REFERRAL BY  
3 COUNSEL FOR COPYRIGHT OWNERS

4 MR. COHEN: Thank you, Your Honor.

5 I think it's clear that in response to  
6 the questions of the Court, Mr. Laguarda has  
7 conceded that this is not a pure legal question.

8 If I may, I'd like to respond to each of  
9 the judges' questions that Mr. Laguarda has  
10 responded to as a way of demonstrating that.

11 Judge Roberts, you asked if there was  
12 agreement on the meaning of streaming. There is  
13 not. And what we have done and what the RIAA has  
14 done is to propose rates for existing subscription  
15 business models that involve interactive streaming  
16 without regard to the precise definition of  
17 interactive streaming. And the problem with this  
18 referral, and its conceded on page eight of DiMA's  
19 reply brief, where they say, "Whether certain kinds  
20 of interactive streaming" --

21 CHIEF JUDGE SLEDGE: Let me interrupt  
22 you, Mr. Cohen.

1 MR. COHEN: Yes, sir.

2 CHIEF JUDGE SLEDGE: There was no  
3 provision in this hearing for a reply brief. I  
4 realize something was filed, but that wasn't asked  
5 for and it's not part of our rules.

6 MR. COHEN: If I, nonetheless, may use  
7 DiMA' reply brief because I think it's an  
8 admission.

9 CHIEF JUDGE SLEDGE: They have filed it?

10 MR. COHEN: Yes. "Whether certain kinds  
11 of interactive streaming, such as the ones outlined  
12 on pages five and six of the copyright owner's  
13 opposition, fall within that definition," that is  
14 their definition, their proposed definition of  
15 interactive streaming, "is a question of fact and  
16 not fit for a referral.

17 "Of course, determining whether  
18 interactive streaming constitutes a digital  
19 phonorecord delivery may involve some inquiry into  
20 what interactive streaming is." And therein lies  
21 the problem for DiMA.

22 This is a factual question, and contrary

1 to what Mr. Laguarda has said, referral of this  
2 supposed legal question, which is really a factual  
3 question, will, as you asked, Judge Wisniewski, not  
4 advance the ball very far because we will  
5 demonstrate through the direct case and again on  
6 rebuttal, if there's any controversy, that the  
7 actual interactive streaming services that are  
8 parties to this proceeding fall on the other side  
9 of the line from this hypothetical definition. So  
10 answering the question, if you could answer their  
11 question as a matter of law, which I will address  
12 in a moment you cannot, but answering the question  
13 about whether something that does not leave a copy  
14 accessible on the computer will not save one moment  
15 of court time in this proceeding because we will  
16 demonstrate through their witnesses that for at  
17 least two and perhaps all three of the interactive  
18 streaming services that are parties to this  
19 proceeding, DiMA members, they, in fact, do leave  
20 copies on the computer that are accessible. And  
21 then the issue is what is accessible. Another  
22 reason why this is a mixed question of fact and

1 law, because how is the Register going to determine  
2 what is accessible on the computer, and we dealt  
3 with this in our opposition papers. Is it in a  
4 temporary Internet file? Is it in some other file  
5 on the computer? Do you stream the first time and  
6 then there's a temporary or a less temporary file  
7 reside on the computer so the next time the  
8 recipient so calls streams, it plays from the  
9 computer rather than a new stream coming from some  
10 host site?

11 So these are all factual questions. And  
12 the definition of what is accessible is factual,  
13 and even if it were legal, and it's not, we will  
14 not save any court time because we will prove and  
15 demonstrate and offer proof about what are the  
16 correct rates for the actual services that are in  
17 business that call themselves interactive streaming  
18 services, which is not a defined term. Not only is  
19 there no agreement on it, everybody admits and  
20 concedes that it is a loosely-defined term that  
21 applies to a group of businesses. And there is no  
22 way where the Register could determine that as a



1 pure legal matter, and that makes a big difference  
2 when compared to the Ring Tones Referral.

3 Now, we, of course, argued in Ring Tones  
4 unsuccessfully that the matter should not have been  
5 referred and ultimately tried to persuade the  
6 Register of the Ring Tone question that was  
7 referred involved factual questions. But the  
8 factual questions there related to whether or not  
9 the Ring Tone was a derivative work under  
10 Section 115 and, therefore, outside of the  
11 compulsory license.

12 We all knew what a Ring Tone was. There  
13 wasn't any dispute between the RIAA and the  
14 copyright owners as to what the theme was, which we  
15 said was outside of 115 and they said was within  
16 115.

17 We thought there were factual questions  
18 that needed to be developed to answer that question  
19 precisely, and we have appealed the Register's  
20 decision. But here there's no similar way to make  
21 a referral because nobody has offered a definition  
22 of what is interactive streaming and the issue of

1 is it accessible on the computer -- Judge  
2 Wisniewski, the question that you asked -- is not a  
3 referral of a pure legal question because that is  
4 not a self-defining term, and it is far from  
5 obvious. And there will be evidence developed in  
6 this proceeding as to what is accessible, what  
7 resides on the computer and, therefore, whether  
8 this activity, which we've all loosely called  
9 interactive streaming, constitutes DPDs, as we say,  
10 under 115 or does not constitute 115, as DiMA now  
11 says, under 115. But that requires the development  
12 of a factual question. So it's not a question of  
13 law. It's not a question that will add to the  
14 efficiency of this proceeding. Not one witness  
15 will not testify and no -- and no savings will take  
16 place at all in terms of the court's time because  
17 we have services -- Napster, Rhapsody, Media Net,  
18 the leading commercial interactive services --  
19 which we believe deposit copies one way or another,  
20 and the technology is complicated, but one way or  
21 the another deposit copies on the end user's  
22 computer. So we will save nothing by this referral

1 and --

2 CHIEF JUDGE SLEDGE: Mr. Cohen, you have  
3 answered this question, but let me present it to  
4 you so that I'm very clear on what you're saying.

5 If the determination is made that a  
6 delivery that does not create an audio file that  
7 remains accessible is not a DPD, then there will be  
8 just as many actions in district court to determine  
9 whether an audio file that remains accessible has  
10 been created as there would be without that kind of  
11 thing?

12 MR. COHEN: Yes, Your Honor. And in  
13 addition, we will still be setting rates for the  
14 services that call themselves interactive streaming  
15 services in this proceeding because they fall, we  
16 think we would show as a matter of fact, on the  
17 other side of this somewhat artificial line that  
18 DiMA is trying to draw, and that is a completely  
19 different situation than we found ourselves in, IN  
20 the Ring Tone Referral.

21 We do not have any real world meaning.  
22 It is an abstract definition, it remains accessible

1 on the computer, it finds no home in the Copyright  
2 Act, it finds no definition inside or outside of  
3 the Copyright Act, and the question is can you  
4 answer that as a matter of law. No. Because to  
5 answer the question in a meaningful way and  
6 ultimately to determine if there's any kind of  
7 interactive streaming service that falls outside of  
8 115, and we think not, but to make that  
9 determination is a factual determination and the  
10 evidence should be developed in this proceeding.

11 JUDGE WISNIEWSKI: Doesn't that factual  
12 determination have to be judged against some  
13 standard?

14 MR. COHEN: Which --

15 JUDGE WISNIEWSKI: Go ahead.

16 MR. COHEN: No, Your Honor. Please.

17 JUDGE WISNIEWSKI: Well, the question  
18 then is would it be fruitful at all to inquire as  
19 to what are the essential characteristics of the  
20 DPD and an incidental DPD under the law?

21 MR. COHEN: Respectfully, no, because it  
22 is inherently a factual question, and I think the

1 Copyright Royalty Judges, as contemplated under the  
2 statute and under the regulations, are perfectly  
3 capable of making that legal determination and  
4 applying law to facts as you do in the course of  
5 each of these proceedings. So to ask an abstract  
6 question, even getting past the problem that it's a  
7 mixed question of law and fact, will not guide the  
8 Court in any way because the only intelligent way,  
9 I respectfully submit, to make that determination  
10 is to actually understand what it is that the  
11 services do. What is it that they do? They're not  
12 radio. Mr. Laguarda said they're radio. They're  
13 not radio.

14 The reason why they are interactive --  
15 radio is not interactive -- the reason why they are  
16 interactive is, we will demonstrate, because of  
17 various technologies that allow immediate access to  
18 some kind of file either on RAM or on the hard  
19 drive or a temporary Internet file that is a DPD.

20 There is no way to answer that question  
21 as an abstract legal question. So, with respect,  
22 answering that question will not help us because we

1       won't know whether services fall inside or outside  
2       of that definition and it is an artificial  
3       construct designed by DiMA for some purpose that I  
4       don't fully understand, but it's not even an  
5       industry term of art that it remains accessible on  
6       the computer. That's not a term that's capable of  
7       interpretation by the Register without testimony,  
8       without factual background, without a description.  
9       We're going to have representatives of these  
10      services. We will ask them, the Court can inquire,  
11      as to the technology that is used to transfer music  
12      to the ultimate user. And it makes no sense to ask  
13      that question in the abstract even if you could get  
14      past the ambiguity in their question.

15               Now, if I can turn to the timing point  
16      because it is important because Mr. Laguarda began  
17      his presentation really on the merits of why he  
18      thinks it's clear that interactive streaming, as he  
19      defined it, is not a DPD. But the question I  
20      thought for today was is the referral appropriate  
21      under 354.1 and 354.2 of the regs, and it's  
22      inappropriate for two reasons. One I think I've

1 already covered. There are factual questions.  
2 351.1, the material question, and 354.2, the novel  
3 material question, are reserved for pure questions  
4 of law, and DiMA has conceded and I've argued  
5 already this morning, this is not a pure question  
6 of law.

7 The second infirmity, which Mr. Laguarda  
8 addressed in questions from Judge Roberts, is the  
9 timing question, and that's very problematic I  
10 think both for this proceeding and as a matter of  
11 going forward for us today.

12 DiMA has read as soon as possible out of  
13 the regulations. Their reading is as long as you  
14 can refer a question so it can be completed by  
15 determination consistent with the Register's  
16 obligation to decide within 14 days for material  
17 questions and 30 days for novel questions. Their  
18 reading is as long as you can get there by the end  
19 and as long as the Court has not set a deadline,  
20 it's time limit.

21 Well, that might be an interesting  
22 argument if 351.1 did not say "as soon as

1 possible." And in response to your question, Chief  
2 Judge Sledge, this has been going on for yours.  
3 Everyone knew since 2001 there were, way before  
4 this proceeding was filed, that there was a  
5 potential legal dispute between DiMA, whose members  
6 have actually launched their interactive streaming  
7 services by entering into commercial contracts in  
8 which they've admitted, but they now seek a  
9 referral to achieve the opposite end -- they've  
10 admitted in those contracts, and we'll put it into  
11 evidence, although we understand that it's not  
12 binding on Your Honors' determination -- but they  
13 have admitted in the contracts in the deals that  
14 were entered into in 2001 that I will actually  
15 address in my opening, they've admitted that  
16 interactive streaming is an activity that falls  
17 within 115. So they obtained rateless licenses,  
18 they've bickered with us back and forth for years,  
19 there were discussions in the context of potential  
20 amendment to the potential so-called 115 Reform  
21 Bill, which would have clarified this, they allowed  
22 us to go forward and file the case knowing we would



1 seek a rate, knowing that the RIAA would seek a  
2 rate. They sat there when the RIAA filed its Ring  
3 Tone Referral to clarify the matter before the  
4 direct case was filed, and they come and they say  
5 way hoped to settle, so we didn't want to rock the  
6 boat. And with respect to Mr. Laguarda, it has  
7 nothing to do with Christmas.

8 I mean the fact of the matter is there  
9 have been discussions on and off, and I don't think  
10 it's appropriate to use the settlement privilege as  
11 a sword and shield, and I think that's what DiMA is  
12 trying to do by raising these settlement  
13 discussions but shielding the substance of those  
14 discussions from this Court. But it is not  
15 appropriate to use the settlement discussions as a  
16 sword and shield, and even if it were, they say in  
17 their papers on page two of their opening brief  
18 that the discussions continue in earnest even  
19 though they have filed this referral.

20 So there's nothing about the filing of  
21 the referral that necessarily puts an endpoint, a  
22 period on the settlement discussions. So it does

1 not excuse their delay. We're sitting here. We  
2 are opening in a few minutes on interactive  
3 streaming, and DiMA could have filed this and  
4 should have filed this in an orderly way at the  
5 beginning of 2006, certainly no later than when the  
6 Ring Tone Referral was filed, and we could have had  
7 a determination of this question if it were  
8 appropriate. We still would have opposed on the  
9 issues that I've raised today that it's not a pure  
10 question of law, but if it had been referred back  
11 in 2006, we could have shaped our direct case in  
12 reliance on the Register's direction and, instead,  
13 we're talking about a process that if the Court  
14 were to refer the question promptly, given the  
15 timing that's been part of these earlier  
16 proceedings and given the need to have adequate  
17 briefing for the Register and given the fact that  
18 the Register has 30 days to answer a novel material  
19 question of law, we will not have any guidance from  
20 the Register before the first phase of this trial  
21 is done. And allowing DiMA to throw in this motion  
22 at 11:59, whether it's around Christmas or after

1 Christmas, just upsets the orderly presentation in  
2 this case. They have known from before we filed  
3 our case that we would seek rates for interactive  
4 streaming. They knew that the services that  
5 actually filed these individual participants, Media  
6 Net, Napster, which has now withdrawn, and Real  
7 Networks, Rhapsody, are, in fact, interactive  
8 streaming services for which we were going to seek  
9 rates. And to allow them to come in at the end and  
10 say we really hoped to settle just doesn't ring  
11 true and it's not an excuse. They have run  
12 roughshod over the 354.1 requirement that the  
13 motion be filed as soon as possible.

14 CHIEF JUDGE SLEDGE: Any questions?  
15 Thank you.

16 Mr. Laguarda, any brief comments?

17 MR. LAGUARDA: Your Honor, first, with  
18 respect to our reply, we filed it pursuant to the  
19 rules and were not aware that we were not permitted  
20 one. There was certainly one permitted in the Ring  
21 Tone Referral, and if it's appropriate, I would ask  
22 the Court's leave to reconsider not allowing the

1 filing of that reply.

2 CHIEF JUDGE SLEDGE: What ruling? Our  
3 order provided that the parties would respond to  
4 the motion.

5 MR. LAGUARDA: Yes, sir.

6 CHIEF JUDGE SLEDGE: It didn't provide  
7 for anything other than a response to the motion.

8 MR. LAGUARDA: Yes, Your Honor, that is  
9 correct, the order that covered Daubert and motions  
10 with respect to oppositions on relevance grounds.

11 There wasn't an order with respect to  
12 other motions, but that was the understanding that  
13 we had, that the rules provided for the opportunity  
14 for reply.

15 With respect to Mr. Cohen's argument  
16 about timeliness, Your Honor, I do not dispute that  
17 the parties have been aware of this issue. The  
18 fact is that the rules should not be interpreted to  
19 prohibit the parties from attempting to resolve  
20 disputes, and attempting to resolve the dispute and  
21 attempting to settle it took place when it did in  
22 earnest between the parties, and that process was

1 the process that we are representing to you led to  
2 our determination that we would be unable to  
3 resolve it before the case commenced. And we  
4 believed it was important for the Court to have the  
5 opportunity to get the guidance from the copyright  
6 office as to the legal question and so we believe  
7 we are doing it as soon as possible consistent with  
8 the rules.

9 With respect to the legal question, the  
10 statute clearly provides that a digital phonorecord  
11 delivery is the delivery of a phonorecord. That's  
12 the question that the Register must answer. What  
13 is the delivery of a phonorecord? Is a phonorecord  
14 delivered whenever there is a transmission? Is the  
15 simple making of the transmission enough to deliver  
16 a phonorecord?

17 Mr. Cohen makes much about all of the  
18 different technologies that can be implicated, but  
19 it's a simple legal question and a standard that  
20 needs to be set in order to address all of the  
21 facts, and the facts to Mr. Cohen's point are not  
22 in the record. And the rules clearly provide that

1 the direct cases are limited to the written direct  
2 statements of the parties, none of which address  
3 the complicated questions that Mr. Cohen admits  
4 need to be resolved if, if the statute allows for  
5 rate setting for this activity. And so I don't  
6 know exactly what he's contemplating, but there is  
7 no evidence that will be put into the record at  
8 this point in time with respect to this question,  
9 and certainly answering the legal issue first makes  
10 sense so that the parties can address the facts in  
11 an appropriate and efficient manner. Thank you.

12 JUDGE ROBERTS: Let me ask a question,  
13 Mr. Laguarda. If we referred the question of is a  
14 transmission a delivery of a DPD, how could the  
15 Register possibly come back with any answer other  
16 than it depends?

17 MR. LAGUARDA: The Register will provide  
18 guidance as to what must be delivered. So the  
19 answer it depends may be the lay answer, but the  
20 copyright law answer will be very specific. The  
21 copyright law answer will be is transmission alone  
22 delivery of a distribution of a digital phonorecord

1 to an end user. Is transmission enough? What are  
2 the meanings of those legal terms, those terms in  
3 the statute? The answer may well be it depends, as  
4 it was in Ring Tones, it depends. But the guidance  
5 is important to answer the question properly.  
6 Without the guidance we're going to go on a wild  
7 goose chase to define something currently not in  
8 the record without any parameters, without any  
9 standards and hope for the best. And that is a  
10 worse outcome than the inconvenience of the motion.

11 JUDGE ROBERTS: Well, I think I hear you  
12 saying now that you're not really looking for the  
13 Register to define what is an interactive stream,  
14 you're looking for the Register to define the word  
15 "transmission" because the word "transmission"  
16 appears in the definition?

17 MR. LAGUARDA: No, Your Honor, I believe  
18 that as the Court has, or Judge Wisniewski  
19 appropriately inquired with respect to the motion,  
20 the question does involve an understanding of the  
21 activity at a very basic level, what is an  
22 interactive stream. But the answer to the question

1 is the meaning of the statutory terms; delivery,  
2 digital phonorecord, distribution. Those are  
3 statutory terms that the Register can answer with  
4 respect to their meaning. And the definition of  
5 streaming in the motion is a way to address it.  
6 That's why the question is there, because it comes  
7 up in that activity.

8 JUDGE ROBERTS: And what about the word  
9 "transmission"?

10 MR. LAGUARDA: I believe that the word  
11 "transmission" has a definition.

12 JUDGE ROBERTS: So you're saying that she  
13 can expand upon that or give some particulars to  
14 that?

15 MR. LAGUARDA: No, Your Honor. The  
16 question is whether a transmission of a sound  
17 recording that does not result in a phonorecord  
18 being delivered to an end user is subject to rate  
19 setting here. It's not the transmission. It's  
20 whether the user is getting a phonorecord.

21 JUDGE ROBERTS: That's what I thought you  
22 said originally and then it sounded as if you were



1 focusing --

2 MR. LAGUARDA: I'm sorry.

3 JUDGE ROBERTS: -- on the word  
4 "transmission" in your --

5 MR. LAGUARDA: No, I'm not focusing on  
6 that word.

7 JUDGE ROBERTS: Okay. All right.

8 CHIEF JUDGE SLEDGE: That last statement  
9 you made, "does it result in a phonorecord," even  
10 if everyone concedes that 115 requires the delivery  
11 of a phonorecord, then you still got the factual  
12 dispute as to whether a specific transmission is a  
13 phonorecord?

14 MR. LAGUARDA: There's no doubt that with  
15 a standard in place there would still be factual  
16 disputes, and that's I believe what Mr. Cohen is  
17 referring to in terms of a record needing to be put  
18 before the Court to decide what actual activity is  
19 implicating digital phonorecord delivery. And his  
20 position is that that activity includes things that  
21 are interactive or things that are not interactive,  
22 and there's a line between the two of them. And

1 Section 114 talks about interactivity. Section 115  
2 talks about digital phonorecord deliveries. That's  
3 the question here. Not interactivity.

4 CHIEF JUDGE SLEDGE: But in this  
5 proceeding, I know you've talked about the limits  
6 of the direct cases presented, but in this  
7 proceeding the services that provide interactive  
8 streaming who are participants or on which we  
9 receive evidence can be resolved factually as to  
10 whether that stream or transmission results in a  
11 phonorecord.

12 MR. LAGUARDA: I'm not sure that we put  
13 forward witnesses -- if the question is can, on  
14 cross-examination or by you or the Court's  
15 questioning, can the particular witnesses from  
16 these services answer --

17 CHIEF JUDGE SLEDGE: No, that's more of a  
18 detailed question than what I'm asking.

19 Notwithstanding the limits at this point  
20 in time as to what evidence can be presented, but  
21 this proceeding has within its context a  
22 determination of services on which evidence is

1 presented as to whether that delivery results in a  
2 phonorecord.

3 MR. LAGUARDA: There are services who  
4 will testify in this proceeding who engage in a  
5 variety of activities, including streaming,  
6 interactive streaming, delivery of permanent  
7 downloads, delivery of conditional downloads.  
8 Those services' activities span a gamut.

9 The issue is whether a particular  
10 activity is subject to rate setting here, and that  
11 question is a question of law as to the boundaries  
12 of Section 115. They may engage in activities over  
13 which there is no 115 rate that can be set, and  
14 that's the meaning of this referral motion.  
15 Whether or not that particular activity by one of  
16 these services is streaming activity, interactive  
17 streaming, streaming, the transmission of a sound  
18 recording to an end user, that does not distribute  
19 a phonorecord deliver a phonorecord to that end  
20 user is subject to rate setting here. But you are  
21 correct that there are parties in this proceeding  
22 who engage in streaming activities, if that's the

1 question.

2 JUDGE WISNIEWSKI: Mr. Laguarda, let me  
3 ask you about the boundaries of your question. If  
4 the facts were to show that an audio file remains  
5 accessible on the client computer beyond the  
6 playing of a sound recording, do you concede that  
7 that, in fact, is a DPD as a matter of law?

8 MR. LAGUARDA: A legal standard needs to  
9 be answered as to what accessible means in this  
10 context, but if accessible means that it is usable  
11 in the way that the statute seems to imply, which  
12 is that it's like a record, like a cassette, then,  
13 yes, absolutely. But the question that needs to be  
14 answered is what is the meaning of that term and  
15 the ambiguity of the term "phonorecord" and the  
16 mere existence of a copy, and perhaps the question,  
17 as Mr. Cohen is referring to it, is for purposes of  
18 infringement or for purposes of technology that  
19 there may be a copy, an instantaneous copy, but is  
20 that the phonorecord Congress intended when it  
21 created this mechanism? Is it just copies that are  
22 made? Any copy? Is Mr. Cohen requesting rates to

1 be set for all Internet transmissions that result  
2 in any copies at any time? No. He's drawn the  
3 line. He's drawn the line in terms of  
4 interactivity. But that's not the line Congress  
5 drew. Congress drew the line in terms of a  
6 phonorecord being delivered to the end user.

7 JUDGE WISNIEWSKI: Well, then haven't you  
8 fell short in terms of the questions that you'd  
9 like to see referred to the Register because you're  
10 suggesting by the answer to the question that I  
11 raised that the Register would have to determine  
12 what does accessibility mean in the legal sense?

13 MR. LAGUARDA: The Register has to  
14 determine what a phonorecord is in this context.

15 JUDGE WISNIEWSKI: You said accessibility  
16 in the legal sense as well.

17 MR. LAGUARDA: There's a definition of  
18 phonorecord in the Act, and that definition applied  
19 here with respect to a delivery of a phonorecord to  
20 an end user is the question.

21 JUDGE WISNIEWSKI: We're going in circles  
22 here, Mr. Laguarda.

1 MR. LAGUARDA: Perhaps I don't understand  
2 the question. I apologize.

3 JUDGE WISNIEWSKI: Let me go back and  
4 take you through the questions that we just went  
5 through. Perhaps we can get to the substance of  
6 this.

7 I said to you if, in fact, the facts were  
8 to show that an audio file remains accessible on a  
9 client computer beyond the playing of a sound  
10 recording, would you concede that such a thing as a  
11 DPD for legal purposes here. You said no, that, in  
12 fact, the Register would still have to determine  
13 legally what the word "accessible" meant. Are you  
14 backtracking now? Does she not have to do that?

15 MR. LAGUARDA: She has to determine  
16 whether or not the user gets a phonorecord, as  
17 intended by the statute. If that means accessible,  
18 then that's part of her determination.

19 The question is whether or not it has to  
20 be accessible, whether or not the phonorecord is a  
21 mere copy, or is the phonorecord what the statute  
22 seems to say it is, which is something that

1 substitutes for, something that does not expand on  
2 rights but is merely comparable to a CD, a record  
3 or cassette. The user gets that and enjoys it like  
4 a traditional phonorecord.

5 Thank you, Your Honors.

6 CHIEF JUDGE SLEDGE: Thank you. We will  
7 recess for ten minutes, so a quarter to the hour,  
8 and then resume with the opening statements.

9 (Brief recess.)

10 CHIEF JUDGE SLEDGE: Thank you. Come to  
11 order.

12 All right. On opening statements,  
13 Mr. Cohen, I believe you will be first.

14 OPENING STATEMENT BY COUNSEL FOR  
15 COPYRIGHT OWNERS

16 MR. COHEN: Thank you. May it please the  
17 court. My name is Jay Cohen. I'm here with my  
18 colleagues from Paul, Weiss, Rifkind, Wharton &  
19 Garrison, and Mayer, Brown & Platt, and we  
20 represent the copyright owners, that is the  
21 songwriters who create the songs that are the  
22 subject of the 115 compulsory license and the music

1 publishers who promote, license and administer the  
2 copyrights in those works.

3 Our clients include two of the largest  
4 songwriter associations in the United States; the  
5 Songwriters Guild of America, which we will  
6 sometimes refer to as SGA, the Nashville  
7 Songwriters Association International, the NSAI,  
8 and the National Music Publishers Association,  
9 NMPA, the largest music publishing trade  
10 association in America.

11 If I could, Your Honor, Mr. Israelite,  
12 who is sitting at the end of the second table, is  
13 the Chief Executive Officer of the NMPA.  
14 Mr. Bogard, next to him, they're all going to  
15 testify, is the head of the NSAI, and Mr. Carnes,  
16 the third person over, is the head of the SGA, and  
17 I think, if I read the transcript correctly, there  
18 was a custom at the beginning to introduce counsel  
19 who will be on their feet. So if I can briefly  
20 introduce the Court to Ms. Bayard, my partner,  
21 Mr. Johnson, and Mr. Brown, who are all from Paul  
22 Weiss, and Mr. Bloch, from Mayer Brown, who will



1 appear as counsel for EMI.

2 CHIEF JUDGE SLEDGE: And, counsel, I  
3 should have mentioned this earlier, to help me and  
4 the court reporter, if all counsel will please  
5 identify yourself as you speak.

6 MR. COHEN: Your Honor, I've given to  
7 counsel for the RIAA and for DiMA, if I may  
8 approach, I have some demonstrative exhibits to use  
9 in connection with the opening. Some of these, as  
10 it's labeled, contain restricted information and  
11 because of the open proceeding, what I will do is  
12 refer the court to the specific tabs without  
13 discussing any of the restricted information so we  
14 don't have to have any issue with respect to the  
15 openings.

16 Now, this is a landmark proceeding of  
17 critical importance for the songwriters and other  
18 copyright owners whose musical works are subject to  
19 the compulsory license.

20 There has not been a litigated proceeding  
21 under Section 115 since 1980, when the rate was  
22 changed from 2.75 cents to 4 cents.

1                   After that litigation, the songwriters  
2                   and music publishers on the one hand and the  
3                   recorded music industry on the other have entered  
4                   into a series of voluntary agreements. The first  
5                   was in 1987, which provided for CPI increases from  
6                   the rate that was in existence after the 1980  
7                   proceeding. It started at 5 cents and went up by  
8                   CPI. And the second voluntary agreement was  
9                   entered into in 1997, which provided for not CPI  
10                  increases per se but step increases every other  
11                  year.

12                  And if the Court will turn to Tab 1,  
13                  where we have summarized those historical rates  
14                  since 1981. The point and the effect is that even  
15                  as a result of these various agreements and step  
16                  increases in the rate, the fact of the matter is  
17                  that the 4 cent rate that was established in 1981  
18                  adjusted for inflation, although not precisely  
19                  intended, essentially yields the 9.1 cent rate  
20                  today. Put another way, the songwriters and music  
21                  publishers have been standing in place with respect  
22                  to the statutory rate for 27 years on an inflation

1 adjustable basis.

2 Now, with all of these prior proceedings,  
3 a 1981 proceeding and the 1987 agreement, dealt  
4 only with physical product.

5 There has never been a proceeding to set  
6 a rate for the digital delivery of music, although  
7 in the 1997 agreement the songwriters and the  
8 publishers agreed with the RIAA that the mechanical  
9 royalty for permanent downloads only -- what we  
10 basically will talk about is iTune downloads in  
11 this proceeding, although iTunes didn't exist in  
12 1997 -- that for permanent downloads the rate was  
13 set by agreement in 1997 at the same rate as for  
14 the physical rate. So today that rate is 9.1 cents  
15 as well.

16 For other types of digital delivery of  
17 music, both conditional downloads and the  
18 interactive streaming that we talked about this  
19 morning, the copyright owners entered into a deal  
20 in 2001 with the RIAA which was essentially, and  
21 I'll talk about this a bit more, essentially was a  
22 rateless deal. It allowed the subscription

1 services, as they have arisen, to develop and  
2 launch in return for some modest advances, the  
3 parties agreed that the rate for those services  
4 would either be set by negotiation, which has not  
5 occurred, or in this proceeding.

6 Now, as I'm sure it's obvious to the  
7 Court from the written direct cases of the parties,  
8 and will no doubt be made clear when counsel for  
9 RIAA and DiMA get up, there is a vast gulf between  
10 the parties as to what constitutes a reasonable  
11 rate for both physical and digital product for the  
12 period through 2012, which is at issue in this  
13 proceeding. And what I've tried to do for the  
14 convenience of the Court in Tab 2 is to summarize  
15 two pages, in tabular form, the rates that the  
16 parties are seeking. And as you can see from Tab  
17 2, there really is a tremendous group.

18 The songwriters and music publishers,  
19 who, as the evidence will show, their mechanical  
20 revenues have not been keeping pace with the step  
21 increases in the rate, are seeking an increase in  
22 the mechanical rate for physical product to 12

1 and-a-half cents per song.

2 The RIAA, on the other hand, proposes a  
3 percentage of revenue rate, but we should not be  
4 confused by the expression of that rate as a  
5 percentage of revenue. In fact, as I set out in  
6 Tab 2, they are seeking a draconian reduction and  
7 their percentage of revenue rate on a penny basis  
8 is 5 cents; the rate that was in effect in 1986,  
9 putting to one side inflation.

10 On the digital side we are seeking on  
11 permanent download an increase from 9.1 cents to 15  
12 cents per download for the reasons and under the  
13 economic theory that I will describe in a few  
14 minutes.

15 Again, the positions couldn't be more  
16 different. If we turn to Tab 4, what the Court  
17 will see is that when the positions of the RIAA are  
18 translated into cents instead of a percentage of  
19 revenue and when the DiMA rate is translated into  
20 cents as opposed to a percentage of revenue, what  
21 the RIAA is seeking for digital downloads is  
22 slightly in excess of 5 cents a song, a little more

1     than half the current rate, and what DiMA is  
2     seeking on a percentage of revenue basis for  
3     digital downloads is a reduction to 4 cents, less  
4     than the current rate.

5             And with respect to conditional downloads  
6     and interactive streaming and Ring Tones, and I  
7     will address all of them in my opening, RIAA and  
8     DiMA are seeking similarly bargain-basement rates  
9     for other types of digital delivery that would, in  
10    essence, choke off the trickle -- what is now a  
11    trickle, but will choke off the mechanical royalty  
12    payments to the songwriters.

13            Now, the impact of their proposals on  
14    songwriters and the other copyright owners would be  
15    ruinous. Because of piracy, a lot of which we will  
16    discuss today, and other factors, the current  
17    rates, although they provided for step increases,  
18    have not resulted in an increase in mechanical  
19    royalties that was expected at the time the parties  
20    entered into their 1997 agreement.

21            As the heads of the two songwriter  
22    groups, Mr. Carnes and Mr. Bogard will testify

1 songwriters in particular have borne the brunt of  
2 this shortfall in mechanical royalties. Although  
3 there are a limited number of success stories, and  
4 to some extent Mr. Carnes and Mr. Bogard are  
5 success stories in the songwriting business, few,  
6 if any, songwriters make a lot of money being a  
7 songwriter, and even for those who support  
8 themselves being professional songwriters, their  
9 lot is a hard one.

10 What they will testify to and what the  
11 other songwriters who will testify in this  
12 proceeding will explain to the Court is that even  
13 at the current rates with step increases, the  
14 declining number of sales of songs has resulted in  
15 account royalties that have not met their  
16 expectation, that have not kept pace with the  
17 increases under the statutory rate and, if not  
18 turned around in this proceeding, will undermine  
19 one of the principal purposes of this proceeding,  
20 which is to maximize the availability of creative  
21 works, because as they will explain to the Court,  
22 if this trends continues, we'll soon be out of

1 songwriters.

2           Now, I mentioned the songwriters at the  
3 beginning because if you review the submissions by  
4 DiMA and the RIAA in this proceeding, you would  
5 think that this was merely a dispute between record  
6 labels on the one hand and music publishers on the  
7 other. And, in fact, Mr. Smith this morning said  
8 he would go after the music publishers. But this  
9 is not a case, and I do not represent just music  
10 publishers, this is not a case solely between  
11 corporate music publishers who are copyright owners  
12 and corporate users who are record labels because  
13 at the bottom the parties who will be most affected  
14 by these rates are songwriters who write the songs  
15 that the record labels record and the digital  
16 companies distribute.

17           Now, it's true, and the testimony will  
18 show, that songwriters typically entrust music  
19 publishers with the right to promote and license  
20 and administer the copyrights in the songs that  
21 they create. But the music publishers retain only  
22 a small fraction of the mechanical royalties that



1 are paid, and that fraction is decreasing, whereas  
2 historically, and certainly at the time of the 1980  
3 proceeding, a common deal in the music business was  
4 for songwriters to retain half of the mechanical  
5 royalties and music publishers to retain half,  
6 50/50 deals.

7 What the evidence will show is that the  
8 paradigm today is for songwriters to get 75 percent  
9 of the mechanical royalties and for publishers only  
10 to retain 25 percent. And there will be testimony  
11 that in many deals that rate is moving towards as  
12 high as 90 percent in favor of songwriters.

13 So the real economic party in interest on  
14 the copyright users' side, which is completely  
15 hidden from view in the submission of DiMA and the  
16 RIAA, are songwriters, who get the overwhelming  
17 share of mechanical royalties that are paid.

18 Now, let me turn to reasonable rates, and  
19 we've had the benefit recently of a decision from  
20 this Court in the SDARS that obviously informs what  
21 we're trying to do in this proceeding, and as this  
22 Court is aware, the task is to set a reasonable

1 royalty that satisfies the 801(b) factors. And I  
2 know those factors are well known to the Court, but  
3 just for ease of reference I've set them out in Tab  
4 5. And those four factors, of course, are to  
5 maximize the availability of creative works, to  
6 afford copyright owners a fair return, to give a  
7 fair income under existing conditions to the  
8 copyright users, to assess the relative roles of  
9 the copyright owners and users, to minimize  
10 disruptive impact.

11 Now, as the Court instructed us in the  
12 SDARS' decision, page 32, and, again, I've  
13 excerpted, just so we're all on the same page, the  
14 lang from Your Honor's opinion, "The appropriate  
15 starting point for setting a rate under 801(b), a  
16 reasonable royalty, is to look at the comparable  
17 market royalty rates and these benchmarks should  
18 then be used to set the rate unless the policy  
19 objectives in 801(b) require some kind of diversion  
20 from those rates." And as this Court stated in the  
21 SDARS' decision, and in an admonition that we  
22 intend the follow, the 801(b) factors should not be

1       judged one by one as a beauty contest. The  
2       question is whether these objective factors, the  
3       factors under 801(b) as a whole, require some  
4       departure from marketplace rates. And that is  
5       exactly how we have constructed our rate proposal  
6       for reasonable royalties.

7               The copyright owners determined that the  
8       benchmarks provided by the market, and which I'll  
9       go through in a few minutes, outside of Section 115  
10      licensing require an increase in the current  
11      statutory rate for physical product, they require  
12      an increase in the current statutory rate for  
13      downloads, and they require the adoption of rates  
14      for other digital distribution that reflect the  
15      market value of their work.

16             Now, our economist who will testify on  
17      this is Professor William Landes from the  
18      University of Chicago Law School, and he's a  
19      pioneer in the field of law and economics, and he  
20      has compared our proposed rates against market  
21      benchmarks involving the same rights, involving the  
22      same parties, and concluded that the rates sought

1 by the songwriters and music publishers are  
2 reasonable because they fail squarely within, in  
3 fact, at the low end of the range of reasonable  
4 rates, and the evidence will show that there are no  
5 policy factor under Section 801(b) that would  
6 require this Court to depart from those market  
7 comparables.

8 So what I would like to do is go through  
9 our rates one by one and explain what the market  
10 comparables are. And, again, for the ease of the  
11 Court, I've set out our rates separately in Tab 7,  
12 and I'll begin with our rate for physical  
13 phonorecords, which is the 12 and-a-half cent rate.

14 The key difference -- really two key  
15 differences between our proposed rate for physical  
16 product and that proposed by the RIAA is that we  
17 are seeking an increase, they're seeking a cut in  
18 half, and we are proposing to maintain the penny  
19 rate structure that has been in place for a hundred  
20 years as a way of measuring the appropriate royalty  
21 rate, and they are proposing a percentage of  
22 wholesale revenue.

1                   Now, fundamental to our request for an  
2           increase is that since 1997, because of  
3           developments in this industry, statutory mechanical  
4           royalties have not kept pace with the actual step  
5           increases in the royalty rate.

6                   What the evidence will show is that the  
7           emergence of all these digital technologies that we  
8           began to talk about this morning has spawned lots  
9           of new methods of distribution ranging from  
10          permanent downloads to limited downloads to  
11          interactive streaming to Ring Tones, and those  
12          digital delivery mechanisms have transformed the  
13          recording music business and they've allowed record  
14          companies to sell their product without the high  
15          costs of physical manufacture and distribution  
16          because CDs aren't pressed, CDs aren't shipped, and  
17          they're not sold on the digital side at traditional  
18          retail stores.

19                  But here's one thing that the parties  
20          actually agree upon in this proceeding: The  
21          outbreak of piracy, of illegal music. Since the  
22          beginning of the digital age there has been a level

1 of piracy that is unprecedented in the recording  
2 music business.

3 The impact on all of the parties, record  
4 labels, music publishers and songwriters alike, has  
5 been severe. The songwriters and music publishers  
6 have been hard hit by piracy because it has  
7 undermined one of the fundamental bedrocks of prior  
8 statutory rate making that publishers and  
9 songwriters would be paid on every copy of a song  
10 that was in distribution.

11 The fact of the matter is, is that there  
12 are countless millions of songs that consumers are  
13 listening to every day which are obtained illegally  
14 and for which copyright owners, songwriters and  
15 music publishers receive nothing under the  
16 mechanical license.

17 Now, when the music publishers and  
18 songwriters agreed to the rate that became the 91  
19 cent rate in 1997, the expectation of those  
20 copyright owners was that they would be paid a  
21 penny on virtually every copy of every song and all  
22 the parties agree no one foresaw the immense amount

1 of piracy that has occurred in the digital age and,  
2 as a result, the expectations of the copyright  
3 owners with respect to what would happen with  
4 respect to sales when they entered into the 1997  
5 agreement has not been met. I think that that is  
6 graphically demonstrated in Tab 8.

7           Tab 8, which is extracted from the report  
8 of one of our experts, shows, and this is  
9 restricted information, what has happened with  
10 wholesale revenue over time in the recording music  
11 business. And if the Court looks at the time of  
12 the last agreement, which was 1997, what it sees is  
13 that with some dips and some changes for more than  
14 a decade that rate of increase of revenue and,  
15 therefore, the number of songs that were going to  
16 be paid mechanical royalties had increased  
17 dramatically, and that continued to about 2000.  
18 And from 2000 forward largely, but maybe perhaps  
19 not exclusively as a result of piracy, there has  
20 been a significant decline in industry revenues.  
21 That has upset one of the fundamental assumptions  
22 on which the 1997 rate was set or agreed to at

1       least from the songwriter and music publisher side.

2               What the evidence will show, and among  
3       other witnesses, you will hear from the chairman of  
4       the NMPA, Irwin Robinson, a long-time publisher who  
5       was one of the principal negotiators of the 1997  
6       agreement, what you will hear is that their  
7       expectation in 1997 was the same that it had been  
8       in 1987, that we were in a digital boom era -- CD,  
9       rather, boom era in which revenues would continue,  
10      the number of songs sold would expand, and while  
11      the actual penny rate that was agreed to was not as  
12      high as songwriters and publishers might have liked  
13      and probably not as low as the record labels would  
14      have liked, that whatever shortfall there was on a  
15      unit basis would be made up on volume. And now  
16      what's crystal clear is that that is not going to  
17      occur on the digital side, and since 2000 there has  
18      been a material decline in the number of CD sales,  
19      meaning that there had been a shortfall in the  
20      mechanical royalties and that the expectations, at  
21      least on our side, and I think on both sides, of  
22      the 1997 agreement have not been met.



1           There's a second piece of evidence that  
2       the Court will hear that has been undermining the  
3       effect or the impact of --

4           JUDGE WISNIEWSKI: Mr. Cohen --

5           MR. COHEN: Yes.

6           JUDGE WISNIEWSKI: How are those  
7       expectations relevant to what we consider?

8           MR. COHEN: Well, I think that the  
9       parties' agreement in 1997, in looking at what the  
10      current statutory rate is, is relevant.

11          JUDGE WISNIEWSKI: In what sense? I mean  
12      how is that going to help us determine the rate?

13          MR. COHEN: I'm going to come to the  
14      benchmarks, but I think what it shows is that it  
15      shows --

16          JUDGE WISNIEWSKI: That's fine. I will  
17      wait.

18          MR. COHEN: The historical context. I  
19      will come to the specific benchmarks.

20          There is a second piece of evidence that  
21      is important in terms of understanding how the  
22      current mechanical rate works, and that's what's

1      called the control composition clauses. And  
2      although the statutory mechanical royalty is 9.1  
3      cents today, the record companies have long sought  
4      to reduce the mechanical royalties by imposing on  
5      their recording artists controlled composition  
6      clauses. Those are agreements between record  
7      companies and recording artists that say if you  
8      record an album for us, if you record a CD for us,  
9      we will not pay the full statutory rate, we will  
10     cap the statutory rate, we will reduce it in  
11     typically in one of two ways. Either by limiting  
12     the number of songs on which a mechanical would be  
13     paid or imposing on the album a fraction of the  
14     statutory rate. We'll pay 75 cents -- 75 percent  
15     of the existing mechanical rate. However applied,  
16     either one of these two ways or in other ways, the  
17     effect has been to reduce the actual mechanicals  
18     that are paid to songwriters and music publishers  
19     below the statutory rate.

20                     Now, let me talk a little bit about  
21     investments made both by songwriters and music  
22     publishers in creating musical work because there's

1       been a lot of discussion on the other side of the  
2       table about music publishers and songwriters really  
3       don't contribute.

4               We are going to present testimony of a  
5       number of talented songwriters and they will tell  
6       you about the personal and financial sacrifices and  
7       the sweat equity that's being discounted on the  
8       other side that they put into creating the songs  
9       that are recorded. And what they will tell you and  
10      explain to the Court is that for songwriters, even  
11      hits produce only modest returns, and the hits are  
12      few and far between.

13             On the music publisher side, one of the  
14      underlying reasons for our seeking an increased  
15      rate is the substantial investment that music  
16      publishers make in developing the creative works  
17      that are recorded by the record companies.

18             Now, what the RIAA will do is they will  
19      parade into this courtroom witness after witness  
20      who will simply refer to music publishers as  
21      passive coupon clippers who don't do anything other  
22      than administer licenses, collect royalties, and

1 allocate checks to songwriters.

2 Presumably this testimony is going to be  
3 offered to persuade the Court that the RIAA wins a  
4 third of the 801(b) factors for relative  
5 contributions of parties.

6 The evidence is all to the contrary, and  
7 we will present the evidence from a number of --  
8 testimony from a number of music publishers. They  
9 will testify about the important and material  
10 contribution that songwriters make to the creation  
11 of the musical works that the record companies  
12 record that the digital distribution companies will  
13 sell, they will tell the Court that they spend tens  
14 of millions of dollars scouring for talent, finding  
15 songwriters, supporting songwriters, they promote  
16 songs, they protect the copyrights in songs, they  
17 license the songs. And what you will hear, which  
18 is perhaps most relevant to that factor, is that  
19 the music publishers advance hundreds of millions  
20 of dollars in advances against royalties to  
21 songwriters. And although it is true that those  
22 advances are recoupable, what the evidence will

1 show both qualitatively and quantitatively is that  
2 a substantial amount of the advances that are made  
3 by music publishers are written off because the  
4 songwriters can't earn them back.

5 So for the RIAA to suggest that all of  
6 the risk is on their side and none of the risk is  
7 on the music publisher and songwriters' side will  
8 not be borne out by the evidence.

9 Now, Judge Wisniewski, now I will turn to  
10 Professor Landes' benchmarks, and he is, as I've  
11 said, at the University of Chicago Law School, he  
12 is the co-author with Judge Richard Posner, a book  
13 entitled "Economic Structure of Intellectual  
14 Property Law," and many other scholarly  
15 publications. And he has spent his entire career  
16 thinking about the issues that are before this  
17 court and writing about those issues.

18 First what he will say is that a  
19 reasonable royalty must be adequate to create  
20 incentives for songwriters to create musical works.  
21 Not surprising since it's the first factor in  
22 801(b).

1                   Moreover, as he will testify as a matter  
2     of economic theory and as a matter of actual  
3     evidence, the statutory rate acts as a ceiling on  
4     what songwriters and music publishers can obtain in  
5     the market. That's not to say, and we're not  
6     suggesting, that you can set the statutory rate  
7     anywhere you want because the parties can bargain  
8     under that statutory ceiling. We understand, and  
9     will -- they will argue for rates that fall within  
10    a range of reasonableness based on benchmarks.

11                  But what Professor Landes' first  
12    observation is, is that because you can bargain  
13    below the statutory rates, and the evidence will  
14    show that music publishers and songwriters have  
15    historically granted licenses below the statutory  
16    rates, because you can bargain below but no  
17    bargaining takes place above, it's important in  
18    setting the rate to be mindful not only of the  
19    range but where in the range a reasonable rate  
20    falls.

21                  Here's what he does, and I'll try to walk  
22    through his analysis in the context of the physical

1 product of the benchmarks that he uses apply to all  
2 of our rates.

3 Now, as the court explained in SDARS, the  
4 key is to select benchmarks that are comparable.

5 What Professor Landes has done is he has  
6 examined benchmarks in the free market outside of  
7 Section 115 in which licensees are seeking both the  
8 right to use the song that's conveyed now by the  
9 compulsory license and the right to use the  
10 recording of that song, the master recording right  
11 that belongs to the record labels. And he  
12 concludes that if he can find transactions in which  
13 both sets of rights are licensed either separately  
14 or together, they provide the best evidence of a  
15 comparable benchmark.

16 So where does he start? He starts in the  
17 Ring Tone market. And the largest number of  
18 voluntary transactions about which you will hear  
19 come from the Ring Tone and master tone market.

20 Now, as we discussed this morning, there  
21 was a referral on Ring Tones and the Register has  
22 concluded for the purpose of this proceeding that

1 Ring Tones fall within Section 115. That referral  
2 was the culmination of a long dispute between the  
3 copyright owners and the record labels with respect  
4 to whether or not Ring Tones were covered by the  
5 compulsory license.

6 Now, although the Register has ruled now  
7 in 2006 that Ring Tones are covered, there were  
8 hundreds of market transactions involving Ring  
9 Tones that predated the Register's ruling, and each  
10 of the music publishers who will testify will  
11 discuss with the Court the rates that they have  
12 obtained, any market transactions for Ring Tones,  
13 and those are set out graphically at Tab 9.

14 And what this shows and what we will  
15 demonstrate is that in the freely negotiated Ring  
16 Tone market, which are snippets of the very songs  
17 that are the subject of the compulsory license and  
18 which the Register has now concluded are subject to  
19 compulsory licenses, the rates that music  
20 publishers obtain in the free market range from 10  
21 to 15 percent and there are penny minimum, which  
22 I've not set out here, but the evidence will show



1       which are well in excess of the current statutory  
2       rate.

3               Now, Professor Landes has also analyzed  
4       agreements directly between record companies and  
5       music publishers with respect to these Ring Tones,  
6       and those agreements are the so-called New Digital  
7       Media Agreements -- New Digital Media Agreement,  
8       NDMA. There will be a lot of testimony about the  
9       NDMA's in this proceeding.

10              Those were a series of agreements entered  
11      into between music publishers representing the  
12      songwriters and major record labels that allowed  
13      the record labels to license Ring Tones to cell  
14      phone companies and other sellers of Ring Tones and  
15      to license both the recording, which they  
16      controlled, and the underlying composition, which  
17      the songwriters and music publishers controlled.

18              So now we have a set of voluntary  
19      agreements between record labels and songwriters  
20      and music publishers with respect to the precise  
21      right at issue here.

22              Now, they've been marked as restricted,

1 but I will ask the Court to turn to Tab 10, and  
2 there'll be a lot of testimony about this, which  
3 summarize those terms.

4 The key number, and provides the bottom  
5 end of Professor Landes' range of benchmarks, is  
6 the middle number which deals with wholesale  
7 revenue. And what we have here is an agreement  
8 between record companies and music publishers that  
9 say to the music publishers we will pay you on the  
10 greater of one of these three metrics: A  
11 percentage of retail revenue, which in the market  
12 is typically a \$1.99 to 250, that's what Ring Tones  
13 sell for -- the math is not too hard from that --  
14 or 20 percent -- I apologize -- a percentage of the  
15 revenue that's received by the record company,  
16 wholesale revenue, or a penny rate minimum.

17 And what Professor Landes does is he  
18 examines those agreements, he examines the many,  
19 many, many Ring Tone agreements that predate those  
20 agreements, and he says that is the bottom of my  
21 range of reasonableness, my market comparables, and  
22 that's set out in Tab 11.

1                   So where's the top? Because without a  
2       top this couldn't be the bottom. The other  
3       principal set of market comparables that he  
4       examines come from the synchronization market. And  
5       the synchronization licenses, as I know the Court  
6       is aware of from prior proceedings, are licenses in  
7       which someone who is making a television show or a  
8       movie needs the right, which is not covered by any  
9       compulsory license, to synchronize music with  
10      audiovisual product. And what he finds, and there  
11      will not be any dispute with respect to this fact,  
12      is that in that market when purchasers of both sets  
13      of rights need both the song and the recording, the  
14      song and the recording share on a 50/50 basis. So  
15      50 percent from that market comparable is the top  
16      of his range, and there are literally thousands and  
17      thousands and thousands of those agreements, all of  
18      which, the way that the 50/50 split is  
19      accomplished, is that both the record label and the  
20      music publisher or songwriter enter into MFN  
21      agreements, Most Favored Nations agreements which  
22      guarantee that they get the same amount.

1                   So based largely, but not exclusively,  
2           but for the purposes of the opening, largely on  
3           these two sets of benchmarks which bracket his  
4           range, he concludes that royalty rates in this  
5           range are reasonable. That is, if compositions of  
6           music are paid between these two ends of the range,  
7           a percentage of the overall revenue -- the revenue  
8           is split for both the recording and the  
9           composition -- anywhere in this range between the  
10          bottom that is implied by the Ring Tone licenses  
11          and the NMDAs and the top, which is applied by the  
12          synchronization licenses, that that is a reasonable  
13          ratio that allows him to conclude that the rate is  
14          consistent with the market comparables.

15                 So how does that work with respect to our  
16          proposed royalty rates? Let me start with the  
17          physical rate. Our physical proposal is for 12  
18          and-a-half cents per song. And if the Court will  
19          examine Tab 11, what we see is that the proposed  
20          rate for physical is near the bottom of the Landes  
21          range.

22                 When one takes into account how much is

1     paid for the recording and how much is paid for the  
2     underlying composition at our proposed rates, the  
3     rate falls at the very bottom of the range implied  
4     by the Ring Tone to synchronization range.

5             As a result, what he will conclude as a  
6     matter of economics is that the rate is reasonable  
7     because it falls within the benchmark of market  
8     comparables.

9             Now, what did the labels propose instead?  
10    Based on a flawed benchmark from the 1980  
11    proceeding that was the subject of our in limine  
12    motion, and I'm not going to go through it in any  
13    detail now, they have come up with a rate which  
14    translates to 5 cents, and the only benchmark on  
15    which they draw for their 5-cent rate is this  
16    analysis, which I think is a misreading, and I  
17    think we will demonstrate to the court is a  
18    misreading, of the 1980 CRT decision. And they  
19    take what they claim is a retail percentage of  
20    revenue rate that was set by the CRT in 1980, even  
21    though, in fact, the rate was a penny rate, and  
22    they convert it into wholesale percentage and they

1 say that's the appropriate percentage to be applied  
2 not only to physical but to be applied across the  
3 board, 7.8 percent of revenue, which is a nickel.  
4 Needless to say we would need another sheet of  
5 paper to see how far below the range of reasonable  
6 benchmarks that proposed rate falls.

7 So what's their justification? Because  
8 apart from the precise rate, the entire RIAA effort  
9 to drive down the mechanical rate hinges -- hinges  
10 on their claim that the recording music industry is  
11 in economic distress. That's the claim.

12 Now, that's not a new claim because the  
13 same set of claims of the rates, as I've said, are  
14 back-to-the-future rates that they're proposing,  
15 they want to go back to the nickel rate 25 years  
16 ago. The argument is also a back-to-the-future  
17 argument because in Tab 13 I have quoted from the  
18 Copyright Royalty Tribunal decision of 1980 because  
19 every argument that will be made by the RIAA in  
20 this proceeding about economic woes of that  
21 industry was made and rejected in the 1980  
22 proceeding.

1                   So what did the Court say in this  
2       passage, the tribunal say? "We note that the  
3       record industry claims that an increase in the  
4       statutory mechanical rates will bankrupt great  
5       record companies and will force others to  
6       drastically cut their operations. We reject all of  
7       these claims, as we find no probative evidence in  
8       the record to support them." And, respectfully,  
9       what I suggest is that at the end of this  
10      proceeding this Court will reach the same  
11      conclusion. There is no basis in economic evidence  
12      that would entitle the RIAA to a mechanical rate of  
13      half of a current rate and a tiny fraction of what  
14      the benchmark ratios imply.

15               Now, we're going to prove this out of the  
16      documents of the RIAA and through our expert  
17      witness, Helen Murphy. Ms. Murphy is not a  
18      stranger to the recording music industry. She was  
19      the chief financial officer of two of the major  
20      record companies. Most recently she was the chief  
21      financial officer of the Warner Music Group, which  
22      is one the four remaining majors, and in the 1990s

1 she was the chief financial officer of Polygram  
2 Music, which has been absorbed into Universal. And  
3 what she will testify to is that although there has  
4 been a decline in top-line revenues, and we saw  
5 that in that earlier chart, the earlier graph that  
6 I directed the Court to, while there has been a  
7 decline in top-line revenues over the past several  
8 years, the profitability of the recording music  
9 business has increased despite piracy, despite all  
10 of the issues that they will raise, and it is  
11 projected to increase steadily, according to their  
12 own documents, over this period.

13 Now, having engaged in what was,  
14 undoubtedly, painful restructuring to ring some of  
15 the fact out of their operations and because of the  
16 higher profit margins on the digital products, and  
17 I'll talk about that in a moment, the digital sales  
18 yield higher profit margins for the record  
19 companies than physical sales, they are on the  
20 whole, the major record companies, as profitable or  
21 more profitable as they've ever been. And that's  
22 set out in this restricted document, Tab 14.



1                   Tab 14, which is derived from data that  
2                   was given to us by the RIAA, sets out from 1991 to  
3                   2005, the last year for which we actually have the  
4                   full data, from 1991 to 2005 revenues for this  
5                   industry, operating profits for this industry, and  
6                   profit margins for this industry. And what it  
7                   shows is that the profit margins in 2005 were the  
8                   highest in the 15 years for which we have data.

9                   So there's nothing that supports this  
10                  tale of economic woe and there's nothing about the  
11                  economic condition of the recording music industry  
12                  that requires the Court to set a rate that is a  
13                  fraction of the current rate and a fraction of the  
14                  appropriate benchmark rate.

15                  Now, there will be a lot of talk during  
16                  this proceeding as well about economic prosperity  
17                  of the music publishers, and what the RIAA will say  
18                  is publishers are prospering, we're suffering, and  
19                  you have to lower the rates.

20                  Well, forget about the songwriters, and  
21                  we'll talk only about publishers. But, again,  
22                  their evidence on music publishers is as

1 unsupported in meaningful ways as their own  
2 evidence about themselves.

3           The evidence will be clear that from  
4 music publishers and songwriters the mechanical  
5 royalty revenues are not increasing at the rate  
6 implied by the increases in the statutory rates.  
7 So what they will say is don't worry about that.  
8 You, the music publishers and songwriters, you have  
9 other streams of income. You can earn  
10 synchronization license fees, which, of course,  
11 they earn as well, and you can earn performance  
12 royalties under a different set of rights. And  
13 because there have been increases in  
14 synchronization royalties and in performance  
15 royalties, they will say you don't have to do much  
16 with the mechanical rate and it justifies pushing  
17 it down. And I think we will be able to  
18 demonstrate to this Court that that is a misreading  
19 of 801(b), it is the exact opposite of the argument  
20 that Professor Ordover (ph) made to you in the most  
21 recently concluded proceeding in which he testified  
22 and this Court adopted that testimony about the

1 need to get full value for every different right  
2 and every different possible income stream.

3 And equally flawed is the fact that while  
4 it may be true that music publishers as a group and  
5 songwriters as a group are enjoying increased  
6 performance and synchronization royalties, it's not  
7 a one-to-one ratio for individual songwriters who  
8 are dependent upon the count of royalties. And  
9 what we will show over the course of this  
10 proceeding both on our direct case and,  
11 undoubtedly, on rebuttal, in light of the arguments  
12 that have been raised, is that songwriters who earn  
13 mechanicals don't necessarily earn equivalent  
14 amounts of performance royalties, they don't  
15 necessarily earn equivalent amounts of  
16 synchronization royalties, and if you cut the  
17 mechanicals of songwriters because of  
18 synchronization and performance royalties, for  
19 many, many songwriters, those other two streams  
20 will be totally irrelevant or certainly  
21 insufficient to make up the difference.

22 Now, the labels also claim that they need

1 lower rates to bring them in line with rates around  
2 the world. And, again, we have filed an in limine  
3 motion on this issue, and I'm not going to try to  
4 spend a lot of time on it today, but what we tried  
5 to say in the in limine motion is that a proper  
6 analysis of foreign rates, even if it has some  
7 meaning under the 801(b) factors, is a complicated  
8 exercise.

9           You can't simply cherry-pick one or two  
10 countries where you find a rate that you think is  
11 lower than the U.S. rate and say ah-ha, those are  
12 large countries, you should adopt their rates.  
13 Let's ignore -- so let's adopt the rate of the  
14 United Kingdom, let's adopt the rate of Japan,  
15 let's ignore the rate of Germany, it's too high,  
16 let's ignore the rate of France, it's too high,  
17 let's ignore the rest of the rates in Western  
18 Europe. These different countries set rates under  
19 different copyright regimes involving different  
20 rights and involve different marketplaces, and to  
21 draw on foreign marketplaces which involve  
22 different bundles -- often involve different

1 bundles of right. For example, in the U.K. there's  
2 no controlled composition clause, so the rate is  
3 the rate. That's not true here.

4 If we're going to use those as market  
5 comparables, it is incumbent upon the RIAA to show  
6 that the markets are really comparable and do a  
7 detailed analysis, and we're going to have to look  
8 at all of those markets because the evidence will  
9 eventually show that foreign rates are below U.S.  
10 rates in some places and they're above in others.  
11 And the key question is are the markets  
12 sufficiently comparable given the different  
13 copyright regimes and given the different bundles  
14 of rights so that you should look abroad rather  
15 than the domestic free market comparables that we  
16 are urging the Court to use as benchmarks.

17 So what will they say about the Landes  
18 benchmark ratio that's set out in that chart? What  
19 they will say is they were coerced into entering  
20 into the New Digital Media Agreements. What they  
21 will say, but the evidence will not ultimately  
22 support, what they will say is at the time they

1 entered into those NDMAs they wanted to license  
2 some other products that were outside of 115. As  
3 for the Ring Tones at that time, they wanted to  
4 license dual disks, they wanted to license  
5 locked-content product, they wanted to license --  
6 that may or may not have been outside of 115 --  
7 they wanted to license audiovisual product. And  
8 what they will say is they had to enter into these  
9 NDMAs, they, these gigantic record companies, had  
10 to enter into the NDMAs at the rates that you will  
11 hear about that informed the Landes benchmark  
12 because they needed those other products, and we  
13 will demonstrate that that's simply not so. And  
14 what the evidence will show and what is most  
15 important to Professor Landes as an economist is  
16 that the NDMAs do not represent a departure from  
17 the preexisting market comparables. The rates in  
18 the NDMAs are consistent with the preexisting  
19 market comparables and represent a continuation of  
20 that market. Thus, we'll be able to demonstrate  
21 and the evidence will show and Professor Landes  
22 will opine, based upon his economic judgment, that

1 the NDMA rates do not reflect some enhanced price  
2 that the labels paid as a result of their purported  
3 desire to license other product.

4 So what are they going to say about the  
5 top end of our range, the sync markets? You're not  
6 going to hear any evidence that sync agreements are  
7 not 50/50 agreements. Again, they have to fall  
8 back on the coercion argument. They're somehow  
9 forced to enter into licenses at below some  
10 hypothetical market rate because a synchronization  
11 licensee, somebody who wants to put music and time  
12 relation to the song, they will say can bypass the  
13 recording. So they can take less than they would  
14 ordinarily get, they take less than the fair value.

15 The argument doesn't make any sense  
16 particularly because it equally applies to the  
17 song. There is no, with very few exceptions,  
18 there's no reason to use one specific song in a  
19 movie and a television show. There are genres of  
20 songs, there are similar songs, and if the  
21 songwriter were to demand too much, a  
22 synchronization licensee can bypass the song in the

1 same way that they can bypass the recording, and it  
2 happens in the real world when publishers and  
3 songwriters ask too much for their song.

4 The fact of the matter is, and what the  
5 synchronization licenses show and why they provide  
6 the endpoint of the Landes benchmark ratio, is that  
7 in a free market without a compulsory license the  
8 fact of the matter is that licensees who need the  
9 song and need the recording pay equal amounts for  
10 those two rights.

11 CHIEF JUDGE SLEDGE: Mr. Cohen, do the  
12 rules of evidence prevent admission of evidence on  
13 the intent and goals and the negotiations of  
14 parties when an agreement has been reached absent  
15 fraud?

16 MR. COHEN: Well, I think that's a matter  
17 of discretion. For, Your Honors, I think that if  
18 you're asking me can you take parole evidence, the  
19 agreements are clear on their face; is that the  
20 question? I think that's typically a matter of  
21 substantive law rather than parole evidence.

22 CHIEF JUDGE SLEDGE: So absent ambiguity,



1       then all of what you've been describing plus what  
2       Judge Wisniewski asked you about the relevance of  
3       the owners earlier would not even be admissible  
4       evidence?

5               MR. COHEN: Well, respectfully, I think  
6       that's not correct I can answer for two reasons.  
7       First, with respect to these benchmarks, I'm not  
8       offering intent of the parties. I'm offering the  
9       marketplace evidence of what the rates are. So  
10      perhaps I misspoke in the course of my opening, but  
11      the point of the benchmark ratios is to say this is  
12      the ratio between the song and the recorded product  
13      at one end that comes out of agreements and this is  
14      the ratio between the song and recorded product at  
15      the other end. I believe it's the RIAA who will  
16      seek to escape the rates in those agreements by  
17      arguing without intent.

18             With respect to the 1997 agreement and  
19      what the parties intended, it's really intended to  
20      give the Court useful background about how we got  
21      to where we are and why we are today.

22             CHIEF JUDGE SLEDGE: Well, if those

1 matters are as much a part of the evidence as your  
2 opening is indicating, perhaps this proceeding will  
3 be a lot shorter than people expect.

4 MR. COHEN: That would be up to the  
5 Court.

6 I think you will find the evidence  
7 important in understanding how we got to where we  
8 are with respect to the rates.

9 Let me just say one more thing about  
10 physical product before I move on to digital  
11 product, and that is with respect to the structure.  
12 I think, as I've said, at the beginning of my  
13 opening, we propose continuation of the penny rate  
14 structure that's been in place for a hundred years.  
15 Historically, the evidence will show the mechanical  
16 rate hasn't moved the price of product to when  
17 there were multiple physical formats in the market;  
18 records, LPs, CDs and cassettes. The same  
19 mechanical penny rate applied to each one of those  
20 even though they were priced differently in the  
21 market.

22 Moreover, and I think this ties into what

1 the Court said in both Webcasters II and in the  
2 recent SDARS' decision, the penny rate, of course,  
3 is a usage base metric. It moves directly with the  
4 number of units of songs that are sold, whereas the  
5 percentage of revenue range, either wholesale or  
6 retail, but the wholesale rate as well that the  
7 RIAA proposes, is not so directly tied to the use  
8 of music. And, in fact, there will also be some  
9 disruption, Your Honors, as you see when you look  
10 at the written direct case of the RIAA, even they  
11 in advocating a percentage of revenue ask for a  
12 percentage phase-in because they recognize that the  
13 royalty systems will have to be redone to move from  
14 a hundred-year penny rate to a percentage of  
15 revenue.

16 So what the evidence will show in the  
17 aggregate is we are proposing a usage-based metric.  
18 It avoids the measurement difficulties involved  
19 with revenue that the Court has commented on in  
20 prior proceedings and the other side has not  
21 proffered any compelling reason why we should move  
22 off of the penny rate.

1                   So what do they say? What they say is  
2                   they need a percentage of revenue rate, they need  
3                   the flexibility so that they can offer a low-cost  
4                   product and that they can offer new products that  
5                   are not possible in the penny rate regime. And  
6                   what the evidence will show, and Professor Landes  
7                   will deal in the first part of this. Is that the  
8                   copyright owners have historically granted  
9                   concessions from the statutory rate in order to  
10                  allow the introduction of budget product. And the  
11                  evidence will show, and the RIAA will testify, that  
12                  this entire plethora of digital products that have  
13                  been introduced into the marketplace had been  
14                  introduced under the penny rate regime. So the  
15                  burden I think should be high, the typical rate  
16                  will use this base metric, and I don't think the  
17                  evidence will support it.

18                  Let me turn, if I can, and I will be  
19                  briefer with respect to the other rights, to  
20                  permanent downloads. And, again, if you will pull  
21                  from Tab 7, here we are also proposing a penny rate  
22                  of 15 cents per song. It's higher than the rate on

1 physical, but it's a penny rate index for  
2 inflation. And what we mean by a permanent  
3 download is the sale of a song or an album over the  
4 Internet in return for a fixed fee, and in today's  
5 market the overwhelming percentage of those sales  
6 are through the Apple iTunes store.

7 Now, many of the factors that lead to the  
8 need for the increase in the physical rate apply as  
9 well with respect to permanent downloads, and I'm  
10 not going to reference that now. But there is one  
11 factor relating to the structure of the digital  
12 market that requires some discussion and cancels  
13 for a higher rate, and that's this.

14 The historical physical market was an  
15 albums-based market. Songs were sold in bundles of  
16 10, 12, 13, 14 songs, it increased as we moved from  
17 LPs to CDs, and the overwhelming majority of those  
18 sales meant that songs were essentially sold 13 at  
19 a time.

20 In this new digital market, while there  
21 are album sales, the evidence will show that there  
22 has been an unbundling of the sale of music. Songs

1 are increasingly sold one by one as consumers pick  
2 hit singles from albums and buy just the hits and  
3 leave the other 12 songs behind. And what  
4 Professor Landes will testify to is that, as a  
5 matter of economic theory, this unbundling requires  
6 a higher rate for the single-based market in order  
7 to adequately compensate and create the correct  
8 incentives for songwriters.

9 Now, where does it fall within his  
10 benchmarks? If we go to Tab 11, what we will  
11 see -- and, again, there's no real factual dispute  
12 on this -- according to public information, public  
13 information, iTunes, which has about 85 percent of  
14 the market, iTunes pays the record labels  
15 approximately 70 cents on the 99-cent song that it  
16 sells. It sells it online for 99 cents, the record  
17 companies get 70 cents. And the record companies,  
18 which have elected to engage in pass-through  
19 licensing -- they are acquiring mechanical licenses  
20 on behalf of Apple -- it's different than  
21 subscription services -- but here on permanent  
22 downloads the record companies are telling Apple

1     you pay us 70 cents and we will take care of the  
2     mechanical licenses as well.

3             So if we look at the Landes benchmarks  
4     and we say where this 15 cents out of 70 cents fall  
5     on the range of reasonableness based on market  
6     transactions, as to what is the appropriate split  
7     between the recorded music product and the song, we  
8     see it's at the very low end of the range and leads  
9     us to conclude that it's reasonable and it's  
10    consistent with the hundreds and hundreds of Ring  
11    Tone agreements that were entered into in the free  
12    market with respect to the split between the song  
13    and the recording.

14            Now, is there anything in 801(b) that  
15    should require the court to depart from this market  
16    benchmark for permanent downloads? I think one set  
17    of facts bear particular mention and help the Court  
18    answer the question in the negative, which is that  
19    this rate, the rate that we propose will not only  
20    offer a fair return to the copyright owners, it  
21    will allow the copyright users to have a fair  
22    income in existing economic conditions.

1           As I said earlier, and I don't think  
2       that -- with respect to the record labels, the  
3       evidence will show that the labels themselves have  
4       asserted and claimed that their profit margins on  
5       digital product is higher than on physical product  
6       mostly because of the absence of manufacturing and  
7       distribution.

8           Why that's important with respect to the  
9       period that's at issue in this proceeding is that  
10      we are moving to an increasingly digital sales  
11      model in the recording music side.

12           If we look at -- I want to show the Court  
13      one more chart -- Tab 17, what we see is that over  
14      the three years for which we have evidence here,  
15      and this trend is continuing, that basically from  
16      the standing start in the digital business the  
17      business of the recording music companies, the  
18      record labels, is increasingly a digital business,  
19      and it's increasingly a digital business where they  
20      earn higher margins than they do on the physical  
21      side.

22           Now, there may be some testimony in which



1 labels will attempt to persuade you that digital  
2 margins aren't higher, but it is completely  
3 inconsistent with their public statements.

4 If you turn to Tab 16, I have one  
5 quotation which is important because it summarizes  
6 a lot of what the evidence will show. And this is  
7 a public document, and it's from EMI's 2005 annual  
8 report to its shareholders, EMI being one of the  
9 four major record companies. And this is a letter  
10 from Eric Nicolli, who was then the chairman of EMI,  
11 in charge of the entire company worldwide to the  
12 shareholders of EMI, and what does he say about the  
13 digital business? "Certain costs borne in the  
14 physical world such as manufacturing returns and  
15 Pick, Pack, Ship are not relevant for digital  
16 products. For physical products these costs are in  
17 the range of 15 to 18 percent of sales.

18 "While there are some digital specific  
19 variable costs and infrastructure investments  
20 needed to fully pursue the digital opportunity, it  
21 is reasonable to expect that our company will be  
22 more profitable as digital sales grow as a

1 proportion of our business." And we will  
2 demonstrate that this is precisely what is  
3 occurring. And although the industry consensus  
4 from public data is the about \$1 billion digital  
5 music business that exists in the U.S. today, or at  
6 least in 2006, will exceed \$5 billion by 2012. And  
7 we will show the record companies' own forecasts  
8 with respect to the digital business and  
9 demonstrate that on the permanent download side the  
10 increase that we are seeking can be readily  
11 absorbed by them because of their increased profit  
12 margins.

13 Now, what about the DiMA companies? What  
14 about Apple as the permanent download provider?  
15 Since it's launch in 2003, iTunes has dominated the  
16 market.

17 We will submit evidence from an industry  
18 expert, Claire Enders, who has analyzed the  
19 development of the digital market, and as she will  
20 say, and again it's public, Apple has got about  
21 85 percent. And although DiMA will devote the  
22 majority of its case on permanent downloads and on

1 subscription to try to persuade the Court that  
2 somehow the digital services are just getting by,  
3 that is certainly not true for iTunes.

4 And what I've done in Tab 18, and this is  
5 restricted information, is to show you the  
6 magnitude of what the iTunes business has become  
7 both in terms of the number of songs, the revenue  
8 that they're earning, and their contribution  
9 margin. But to talk about the struggling digital  
10 musical companies, and we'll deal with the others  
11 in a few minutes, has no applicability based on the  
12 evidence for iTunes. And what's really remarkable  
13 about iTunes is that this success really seems to  
14 have been unintended because what Apple has said in  
15 statement after statement after statement, and in  
16 Tab 19 I quote an earnings call from the chief  
17 financial officer of Apple from the Spring of 2007,  
18 is that they have said "Our philosophy has been to  
19 run the music store just a little bit over  
20 break-even because we think that selling music and  
21 now videos helps us to sell iPods and accessories."

22 There isn't anything about our proposal

1     that's going to interfere with that business  
2     strategy, and we will demonstrate that  
3     quantitatively and through testimony.

4             Let me turn to limited downloads and  
5     streaming. Again, what we propose here is a  
6     slightly different set of rates, and they're  
7     summarized in Tab 7.

8             What we propose here is a three-part  
9     rate, which is the greater of percentage of revenue  
10    or percent of total content cost fitting into the  
11    Landes benchmark ratio, or fractional penny rate.

12            Now, it would be a lot easier for us if  
13    we could simply apply a simple rate to limited  
14    downloads and interactive streaming. So what is  
15    the reason for this three-part rate and why are we  
16    seeking a different rate structure than the penny  
17    rate that we're seeking for physical and for  
18    permanent downloads?

19            The answer, and it's an important answer,  
20    is the business models are really unsettled and  
21    there are -- typically now the way that these  
22    services charge, and they're typically subscription

1 models, is that the subscription services charge a  
2 set amount to consumers. But the business is  
3 moving. We don't know which way it's going to land  
4 in 2008 to 2012. There's a service called Spiral  
5 Abroad (ph), which you'll hear testimony about.  
6 That's an advertising-based service. There are  
7 some subscription services that charge higher  
8 prices and some that charge lower prices because  
9 they want to drive eyeballs to their website and  
10 earn different revenue.

11 And in these evolving models what we've  
12 attempted to do is to set out rates that mimic the  
13 structure of the rates of the contracts that have  
14 been entered into by the record companies because  
15 what the evidence will show is that the record  
16 companies also have three-part rates in their  
17 voluntary agreements. Because of the uncertainty  
18 of this market, they're not content to take a penny  
19 rate, although they have a penny rate piece;  
20 they're not content to take a percentage of  
21 revenue, although they are have a percentage of  
22 revenue piece; and they're not content to take a

1 per subscriber fee, although they have those  
2 pieces.

3           So what we have attempted to do in this  
4 evolving market is to say that we should be  
5 entitled to the same protection with respect to the  
6 structure of the rate as the record companies who  
7 have entered into these free-market negotiations,  
8 and what we have done is to benchmark what we are  
9 seeking against the total amount that they are  
10 seeking. By saying no more than a third, what we  
11 are saying is that we are seeking a percentage of  
12 the total content pool, the total amount paid for  
13 music, for the recording and for the song that fits  
14 squarely within the Landes benchmark ratio based on  
15 Ring Tone agreements and based on the  
16 synchronization licenses. And, you know, setting  
17 the rate right here is particularly important  
18 because, as you will hear -- we had a little bit of  
19 discussion about this morning -- this industry, the  
20 subscription industry, the interactive streaming  
21 and limited download industry, was launched when  
22 the music publishers and songwriters agreed to

1 rateless deals in 2001.

2 The copyright owners have invested in  
3 this business by essentially giving them a free  
4 license for these past seven years and what's  
5 required now, I respectfully submit, is a rate  
6 based on the benchmarks that gives fair value for  
7 the copyright owners for the investment that they  
8 made in this business that has allowed this  
9 business to begin to develop.

10 Now, what do our opponents say about this  
11 rate? The first thing that DiMA says is they can't  
12 afford it. They can't afford it. They're paying  
13 too much to the record companies to pay a royalty  
14 that we think is implied by the benchmarks to the  
15 owners of the music. And I think our first answer  
16 to that comes from Webcasting, and I think it  
17 applies with particular force here, and it's in  
18 Footnote 7 of the Webcasting decision, which I've  
19 excerpted in the last tab, which is to say, "To  
20 allow inefficient market participants to continue  
21 to use as much music as they want and for as long a  
22 time period as they want without compensating

1 copyright owners on the same basis as more  
2 efficient market participants trivializes the  
3 property rights of the copyright owners."

4           The fact of the matter is that the  
5 interactive streaming services and limited download  
6 services have entered into agreements with the  
7 record labels which have provided for a substantial  
8 percentage -- we'll demonstrate the numbers -- a  
9 substantial percentage of their revenues to be paid  
10 to the record companies. And there is nothing  
11 about rate setting under Section 115 that should  
12 say or does say that copyright owners, because they  
13 have a compulsory license, are relegated to some  
14 table scraps, whatever is left after they've fed  
15 the record companies. It might have been the price  
16 of getting into that business they could not have  
17 entered into rateless deals with the record  
18 companies, but the fact that we did so under the  
19 compulsory license does not mean that we have to  
20 take the bargain-basement rates that they are  
21 proposing.

22           Now, they do offer a rate on the DiMA



1 side for the subscription services, and that is a  
2 4 percent rate. And they will offer the testimony  
3 of their economist, Ms. Karen Calvern (ph), and we  
4 will deal with her testimony, and we have also  
5 raised some issues in an in limine motion, but the  
6 fact of the matter is there is no market benchmark  
7 that supports a 4 percent rate and there is no  
8 market benchmark that supports the multiple between  
9 what they are offering the owners of the songs and  
10 the owners of the recordings and it's way outside  
11 of the Landes benchmark rate.

12 Finally, on Ring Tones, again, our  
13 proposal is in Tab 7. What we're seeking here is  
14 the greater of 15 percent of revenue for a third of  
15 content costs or 15 cents per Ring Tone.

16 This one is an easy one for us at least.  
17 You will hear testimony about all the market  
18 benchmarks. There are many, many, many Ring Tone  
19 agreements.

20 The rates that we are seeking are  
21 supported by those agreements. They are -- in  
22 fact, they are supported on the percentage of

1 revenue side. They are supported on the penny  
2 minimum. In fact, because of the pricing of Ring  
3 Tones, there are many Ring Tone agreements that pay  
4 music publishes and songwriters today penny rates  
5 well in excess of the minimum that we're seeking.  
6 And Professor Landes has looked at these  
7 agreements. They fall clearly within his benchmark  
8 ratio of comparable marketplace agreements, and he  
9 finds them to be reasonable.

10 And before I sit down I want to spend  
11 thirty seconds just talking about one term that we  
12 propose because each of us has proposed certain  
13 changes in terms that are important, and the one  
14 that's important to us -- they're all important --  
15 but the one that I want to mention in the opening  
16 is we are proposing for the first time a late fee  
17 of 1 and-a-half cents per months, as well as a  
18 3 percent charge for pass-through licensing in  
19 situations such as the iTunes situations where the  
20 labels take it upon themselves to acquire the  
21 mechanical license for iTunes rather than iTunes  
22 being licensed directly, and that may be their

1 right under the Copyright Act. I'm not disputing  
2 that. But the fact of the matter is that these  
3 pass-through licenses delay our payments and the  
4 evidence will show that record companies are  
5 chronically late on the payment of mechanical  
6 royalties. And as this Court observed in each of  
7 the last two proceedings of Webcasters II and the  
8 SDARS' proceeding, timely payment is essential to  
9 the statutory scheme, and that's all we're seeking  
10 to achieve through those change in rates.

11 So in conclusion, the evidence will show  
12 that songwriters and music publishers are proposing  
13 rates that are comparable, consistent with market  
14 comparables, they satisfy the objectives of 801(b),  
15 they can be absorbed by the RIAA and DiMA companies  
16 without any disruption of their business, and, by  
17 contrast, what we're being offered in return are  
18 throw-back rates to the 1980s that are wildly  
19 outside of the contemporary market benchmarks and  
20 if those rates were adopted, would wreak economic  
21 havoc on the songwriters who write the songs that  
22 the RIAA companies record and that the digital

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1 companies sell.

2 CHIEF JUDGE SLEDGE: Thank you.

3 I'm sure Mr. Cohen carefully planned his  
4 presentation to end at noon. We will recess until  
5 1:00 o'clock.

6 (Whereupon, at 12:06 p.m., a  
7 luncheon recess was taken.)

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1 CERTIFICATE OF NOTARY PUBLIC

2 I, SHARI R. BROUSSARD, the officer before whom  
3 the foregoing hearing was taken, do hereby certify  
4 that the testimony appearing in the foregoing pages  
5 was taken by me in stenotypy and thereafter reduced  
6 to typewriting under my direction; that said  
7 transcription is a true record of the testimony  
8 given by said parties; that I am neither counsel  
9 for, related to, nor employed by any of the parties  
10 to the action in which this hearing was taken; and,  
11 further, that I am not a relative or employee of  
12 any counsel or attorney employed by the parties  
13 hereto, nor financially or otherwise interested in  
14 the outcome of this action.

15

16

17

18

  
SHARI R. BROUSSARD

19

Notary Public in and for the

20

District of Columbia

21 My commission expires:

22 July 14, 2010

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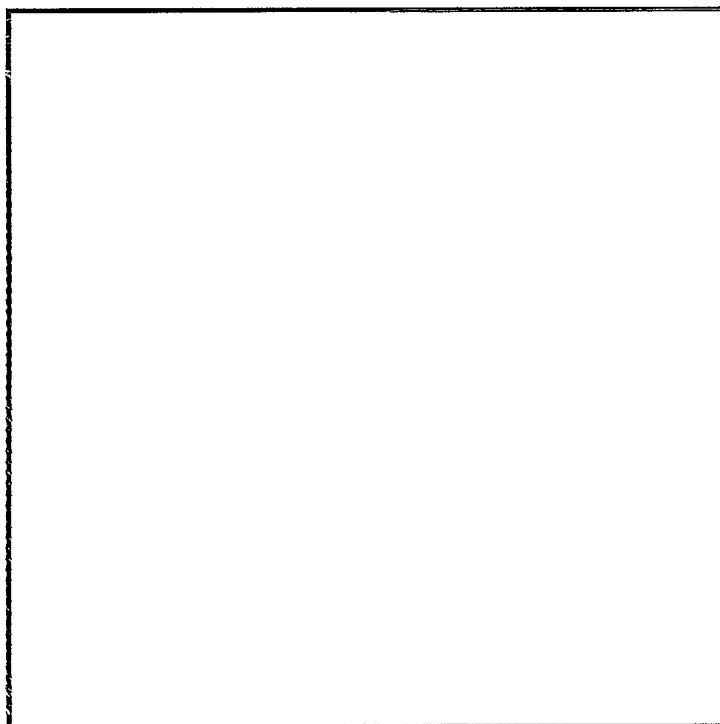
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